07 JUNE 2010

JERÓNIMO MARTINS, SGPS

COMPANY REPORT

FOOD RETAIL

ANALYST: MIGUEL COSTA

The European Retail Star with the right Polish asset....

We have downgraded our PT to €8.12/sh driven by a riskier environment for Equity investments...

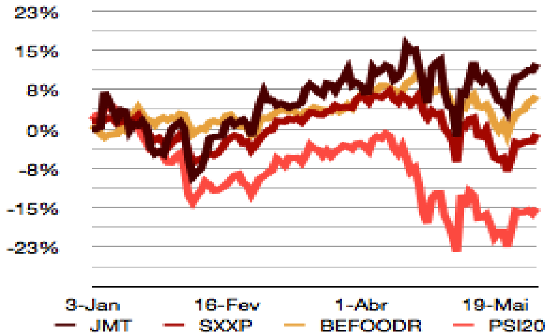
- **Deteriorating macro outlook:** We have updated our DCF assumptions to reflect the riskier environment for equity investments both in Portugal and Poland. **Market Premium for Portugal increased from 5.4% to 6.3%, while in Poland we are now using 7.2% instead of the previous 6.1%**
- **Sales** are expected to grow at a CAGR of 7.1% in the next 10-year period with Jerónimo Martins being much more leveraged to the upbeat dynamics of Biedronka's operations. We highlight that the company's most valuable asset is expected to grow its sales at a CAGR 9.6%[1] in that same period
- **Do not forget Portugal:** Even though the worst than expected macroeconomic environment could affect consumption in Portugal, we remain particularly optimistic with Retail Mainland operations based on: (i) Pingo Doce strong brand awareness and, (ii) restructuring of Feira Nova's operations. **Given the company's stronger focus on food retail, we believe it would be more resilient to declining consumer incomes than its peers, though not completely immune**
- **De-levering process:** We expect the company to gradually decrease its Net Debt due to its strong generation of cash flows and the consolidation of Biedronka's operations
- We have included a new scenario in this report concerning the possible **Poland's Euro Adhesion** in 2015. **According to our analysis, our Price Target would be increased to €10.4/sh amid a stronger exchange rate and lighter valuation assumptions...**

Recommendation:	**BUY**
Vs Previous Recommendation	*Buy*
Price Target FY10:	**8,12 €**
Vs Previous Price Target	*8,78 €*
Price (as of 7-Jun-10)	**7.29 €**

Reuters: JMT.Ls, Bloomberg: JMT.PL

52-week range (€)	4,28-8,31
Market Cap (€mn)	4.229
Outstanding Shares (mn)	628,4

Source: Bloomberg and Nova ER Team



Source: Bloomberg

(Values in € mn)	2009	2010E	2011E
Sales	7.317	8.177	9.051
EBITDA	528.0	597.6	663.4
EBITDA margin (%)	7.2%	7.3%	7.3%
Net Profit	200.3	255.8	289.1
EPS (€)	0.32	0.41	0.46
P/E (x)	21.9	20.0	17.7
RoE (%)	18.8%	21.4%	21.6%
EV/EBITDA (x)	10.33	9.13	8.22
Capital Expenditures (€)	312.0	436.7	511.6

Source: Company Data and Nova ER Team

Company description
Jerónimo Martins, SGPS, S.A. processes, manufactures, and retails food and other consumer goods in Portugal and Poland. The company operates the Pingo Doce, Feira Nova, Recheio and Biedronka store chains. JMT also produces edible oils, spreads, and dressings, and manufactures detergents and household cleaners.
Industry outlook: Defensive
Most of the company's revenues are related to the food retail through hard discount operations. The sector has shown tremendous resilience to macroeconomic cycles.

[1] All *Compound Average Growth Rates* (CAGR) included in this report are Real growth rates, adjusted for the Euro currency whenever related to Biedronka's cash flows

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INVESTMENT CONSIDERATIONS

*We are rating the stock **BUY** with a Price Target of €8.12/sh, strongly supported by 6 key factors, which we now summarize**:***

- **We expect Earnings per Share (EPS) to grow at a CAGR of 8% in the next 10-year period, with the dividend payout gradually increasing to 70% as the company improves its Leverage and Liquidity position;**

- **Both the Polish and the Portuguese retail Modern Grocery Distribution markets are expected to remain growing well above the inflation. The Polish market is expect to growth at a CAGR of 7% in the next five years, while the Portuguese one is expected to grow at a CAGR of 4%. In both markets we expect the company to keep increasing its market share, with sales growing well above the industry average;**

- **We have included a new scenario concerning the possible Polish Euro Adhesion in 2015, which would increase our Price Target from the initial €8.12/sh to €10.4/sh. As Poland delays the Euro adoption the potential upside decreases until it reaches €10.11, considering here 2020 as the real date;**

- **We have also studied a possible *Initial Public Offering* (IPO) for Biedronka, as a last resource option for JMT to finance its new Internationalization process. According to our analysis, such scenario would yield a new PT varying between the €8.19/sh, considering only a 10% sale, to €8.49/sh in the case Jerónimo Martins sells 49.99%;**

- **Brazil is also excluded from a new Internationalization process according to our analysis. Pão de Açúcar, Wal-Mart and Carrefour have already consolidated their presence, decreasing the possibility of Jerónimo Martins to replicate Biedronka's success;**

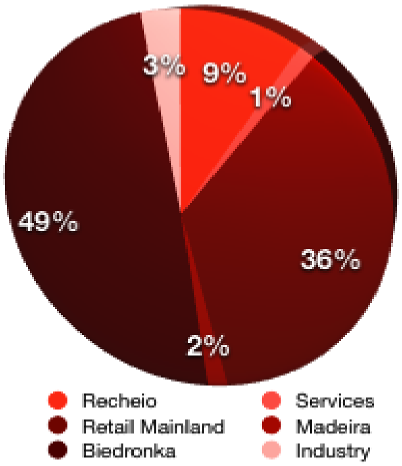
- **The main risk to our *sum-of-the-parts* valuation is the Zloty to face a harder depreciation relatively to the Euro;**

    - ***Mitigating factor –*** *We have used the Forward rates available in the market, which theoretically are the best proxy we can get for the future. Additionally, the Polish Economy is expected to outperform the remaining European countries in the following years.*

Company overview

Jerónimo Martins is the largest retailer in Portugal, closely followed by *Sonae MC,* maintaining also a high growth operation in Poland that is currently the unquestionable market leader. In both countries it owns hypermarkets, check cashing stores and supermarkets.

Exhibit 1 – Sales Breakdown (2009)



Source: Company Data

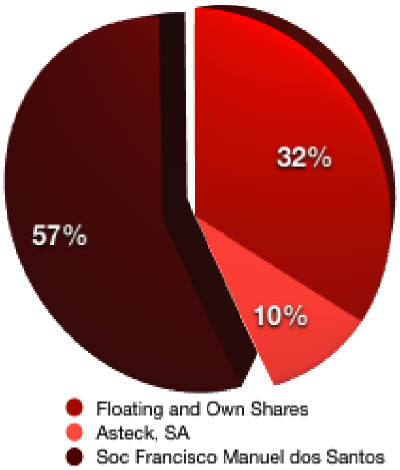
The company's retail banners include **Feira Nova**, **Pingo Doce** and **Recheio** in Portugal. Regarding Poland, the company owns the 1.466-store **Biedronka** hard discount chain, which is by far the largest source of income for the group, representing 72% of its *Net Profit* in 2009. Hard-discount operations represent 8% of the overall Polish retail market, with Biedronka currently dominating 70% of that segment. Additionally, the company owns an **Industry** unit, resulting from a Joint Venture with Unilever, and a **Services** unit, which is involved in the exclusive representation and distribution of international brands.

Finally, we divided the company into the six business units mentioned above, analyzing and valuing each one of them separately.

Shareholder's Structure

The majority of the capital is currently controlled by the **Soares dos Santos** family, which owns 56.1% of the company through *Sociedade Francisco Manuel dos Santos*. Even though more than 30% of the company's capital is currently *free-floating*, the company has other major shareholder: **Asteck, S.A.**, with10%. Finally, **Barclays Capital** recently bought 1.72% of Jerónimo Martins outside the open market, increasing its position to 2.35% and becoming the most recent qualified shareholder.

Exhibit 2 – Shareholders Structure



Source: Company Data

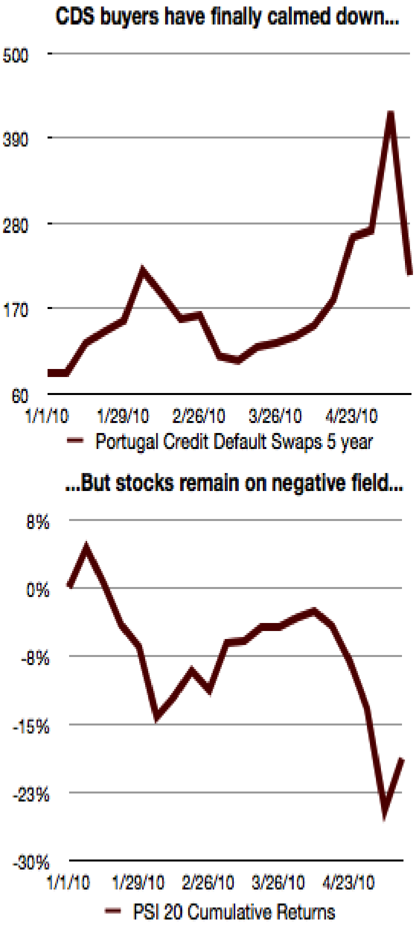
We recall that the company recently surprised the market when its previous CEO Mr. Luís Palha was suddenly replaced by one of Soares dos Santos's family member, Mr. Pedro Soares dos Santos. However, Mr. Luís Palha will remain in the company's board, relaxing investors given its critical role in Jerónimo Martins impressive delivery over the decade. We believe this replacement assures that the company's interest will not be harmed by possible family disputes.

Additionally, the shareholder structure differs in terms of Business Units as well. While Recheio, Services and Biedronka are fully owned by JMT, the same does not apply to Retail Mainland, Madeira and Industry operations. The first one, is 49% owned by the Dutch retailer **Ahold**, an issue we will further analyze in this report.

Regarding Industry, the majority of its capital is in **Unilever**'s hands (55%), while Services is 75% owned by Jerónimo Martins, with the remaining stake being detained by **Lidosol** and **J.G. Camacho**.

Macroeconomic Analysis

Exhibit 3 – Portuguese Macro outlook



Source: Bloomberg

In **Portugal** the Government has racked up record public deficits as it pursued bailouts, fiscal stimulus and public spending in an attempt to revive the at least fragile Portuguese economy. The country now faces increasingly difficult challenges as it tries to boost competitiveness and persistently low GDP growth against the backdrop of a heavy debt burden and significant imbalances. Consequently, the market has perceived Portugal as a risky country with a high probability of incurring in default. **However, we remind that Jerónimo Martins has its focus on the Food Retail sector, mostly through hard discount operations, which makes it less dependent on macroeconomic cycles.** One might argue that Feira Nova, Industry and Services are more susceptible to those cycles, which could eventually harm the company's future growth. Fortunately, the Feira Nova operations are going through a major restructuring process that will lead to an aggressive reduction of non-food related goods. The Services and Industry operations, the most exposed ones to declining consumer incomes, represent only 4% of our *sum-of-the parts* valuation. Therefore, any slowdown in its growth would only have a marginal impact in our Price Target of €8.12/sh.

Conclusion: we maintain our previous statement that the recent economic turmoil has a Neutral impact on the company's growth prospects[2].

The Polish government recently mentioned 2015 as the new target for the Euro adoption...

In **Poland** the Macroeconomic perspectives are much brighter, with economists expecting the Polish economy to keep growing well above the Euro Zone. Despite the fact that it had to postpone the Euro adoption due to larger public deficits and the sharp devaluation of the Zloty, we highlight the fact that Poland recorded the highest real GDP growth among OECD countries in 2009. Furthermore, a recent report issued by the IMF[3] reinforced the growth prospects for the former communist country, forecasting a growth of 2.75% this year and 3.25% in 2011. Considering its recent stoning performance, Poland's debt should stay below 55% of its GDP this year, according to its Finance Minister Jacek Rostowski, therefore well below the 73.6%[4] average in the European Union.

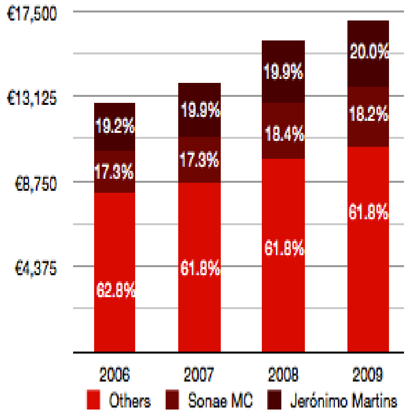
Conclusion: despite the fact that it led to the consequent postponement of the Euro adoption, the measures undertaken by the Government were the appropriate ones as the sharp depreciation of the Zloty cushioned the impact of a foreign shock.

[2] The impact regarding the Cost of Debt is analyzed in the **De-levering Process** part of this report
[3] "World Economy Outlook", April 2010
[4] Source: OECD

Retail Industry Overview

A. PORTUGAL

Exhibit 4 – Portuguese MGD market



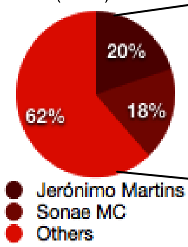
Source: TNS, Planet Retail and Nova ER Team Estimates

The Modern Grocery Distribution (MGD) market in Portugal totals €17.305 mn (2009), with food retail sales accounting for almost half of the overall retail sales. The rationale behind this fact lies on the fact that Portugal is still one of the poorest countries among the UE, with consumers spending a significant part of their income in food-related goods. Portuguese have consumers spent 18% of their overall consumption in food-related goods, which contrasts with 15% in Germany and only 12% in the UK[5].

Market Size and Growth

The food retail market is a highly concentrated one, with the Top 5 retailers accounting for approximately 70% of the overall market. Even though this is in line with other European mature markets, we highlight the fact that both market leaders, Jerónimo Martins and Sonae MC, have market shares close to 20% each.

Exhibit 5 – Market Shares (2009)



Source: TNS, Planet Retail and Nova ER Team Estimates

Exhibit 6 – Market Shares in the Portuguese MGD market

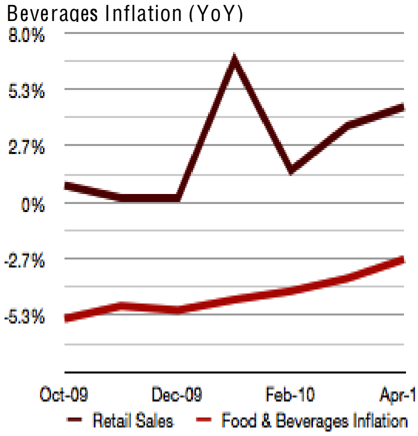
	2006	2007	2008	2009	CAGR
Jerónimo Martins	**2.458**	**2.745**	**3.172**	**3.407**	**12%**
Sonae MC	2.215	2.391	2.930	3.106	12%
Intermarché	1.243	1.393	1.484	1.581	8%
Jumbo	*753*	*n.a.*	*903*	*1.100*	*13%*
Carrefour[6]	*1.110*	*976*	*908*	*915*	*(6%)*
Lidl	n.a.	819	935	957	8%
Others	5.006	5.487	5.624	5.969	6%
Total	**12.785**	**13.811**	**15.955**	**17.305**	**10%**

Source: TNS, Planet Retail and Nova ER Team Estimates

Both retailers have been increasing their market shares, either by organic growth or by M&A operations. We recall that Jerónimo Martins acquired the Plus stores to the *Tengelmann Group* in 2007, reinforcing its leadership in the Portuguese supermarkets' segment and in the Polish hard-discount market. Furthermore, Sonae bought the Carrefour hypermarket operations in 2007, strengthening its leadership position in that segment as well.

This consolidation process increased the weight of both companies in the Portuguese MGD market, a trend that has been obvious in the last three years (see Exhibit 4).

Exhibit 7 –Retail Sales Index and Food & Beverages Inflation (YoY)



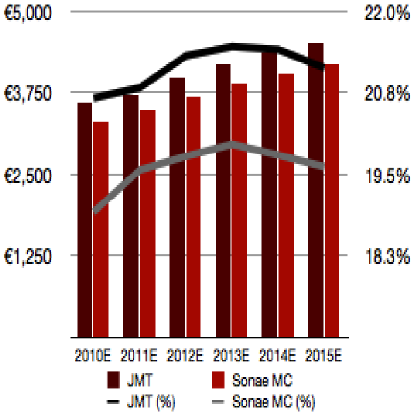
Source: Bloomberg

Though the Portuguese macroeconomic picture remains clearly negative, with the country struggling to fend off the image of a new Greece, we also expect Jerónimo Martins to benefit from a reversion in the deflationary effect that have been hitting retailers since 2009 (see **Exhibit 7**).

[5] Source: Government Data (2009)
[6] Including only the Minipreço operations

Growth prospects

Exhibit 8 – Portuguese MGD forecasts



Source: Nova ER Team estimates

Given the existent wealth gap between Portugal and most of its European peers, we believe there is still room for further growth. We have assumed a slower growth in the following years with the market growing only slightly above the expected inflation rate. The austerity plan followed by the Portuguese Government, combined with high unemployment rates and tougher economic conditions, should lead to a decrease in the consumer spending in the following years. Once the Portuguese economy recovers and consumer income starts rising again, we expect the market to accelerate its growth.

We summarize our growth prospects for the Portuguese food retail market in the following table:

Exhibit 9 – Portuguese MGD forecasts

	2010E	2011E	2012E	2013E	2014E	2015E	CAGR
Jerónimo Martins	**3.592**	**3.714**	**3.969**	**4.181**	**4.366**	**4.499**	**4.60%**
Sonae MC	3.289	3.489	3.682	3.889	4.036	4.176	4.89%
Others	10.504	10.634	10.973	11.420	11.994	12.621	3.74%
Total	**17.385**	**17.834**	**18.624**	**19.490**	**20.396**	**21.296**	**4.14%**

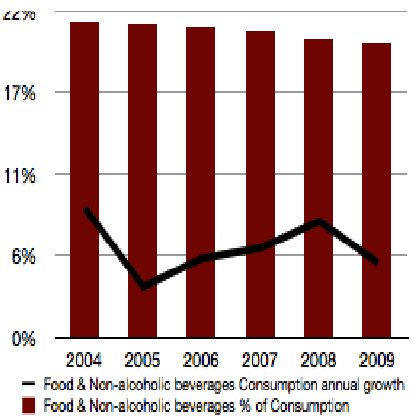
Source: Nova ER Team Estimates

Conclusion: we expect the market to grow at a CAGR of 4.1% until 2015, with both Jerónimo Martins and Sonae increasing their market shares at the expense of other retailers to 21% and 20%, respectively.

B. POLAND

As we see in **Exhibit 10**, the Food & Non-alcoholic beverages consumption as a percentage of Consumption has decreased from 21.2% in 2004 to 19.8% last year. However, recall that German consumers spent 15% of their overall income in Food & Non-alcoholic beverages last year, while British ones spent only 12%. Notwithstanding, such consumption has increased at an average annual growth rate of 5.7%[7] the last decade. **This means that Polish consumers have been allocating decreasing percentages of their incomes to food consumption as their purchasing power increases, leading to different and more diversified spending patterns.**

Exhibit 10 – Retail Sales Index and Food & Beverages inflation (YoY)



Source: Bloomberg

The Polish retail market is also highly fragmented, with as many as 42% of Poles shopping at self-service stores such as supermarkets and hypermarkets, according to a recent study issued by Pentor. **That compares with approximately 70% in Western Europe, which leaves much room left for further growth as the market matures and converges to the Western European standards.**

[7] Source: International Monetary Fund

A recent Euromonitor International report added a new piece of data supporting our previous conclusion by mentioning that as many as 7.000 small groceries closed at the end of 2008, a trend that has becoming stronger as Polish customers abandon shopping at traditional stores, where prices are 20% higher than those of discount stores.

Some of the international retailers are also struggling with their lack of scale...

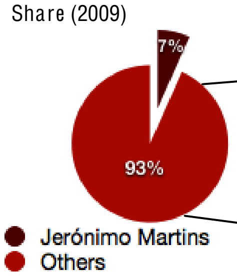
Besides the local retailers, some of the international retailers competing with Biedronka are also struggling with their lack of scale. According to the local press, Aldi has already slowed down its initial expansion plans as it struggles to compete in Poland.

Market Size and Growth

The Polish Modern Grocery Distribution market has been shaped by foreign retailers such as Metro, Jerónimo Martins, Tesco, Carrefour, Schwarz Group, Auchan and Rewe since 2000. Despite some signs of further market consolidation, the Top 5 retailers account for only 21% of the Retail Modern Distribution, well below the level of concentration we see in Portugal (70%) and other European mature markets.

Though we recognise the market a strong potential regarding growth, the Polish grocery market expanded its sales at a CAGR of only 6% since 2006, well behind the 10% exhibited by its Portuguese peer.

Exhibit 11 A – Market Share (2009)



Source: TNS, Planet Retail and Nova ER Team Estimates

Exhibit 12 – Market Shares in the Polish MGD market

	2006	2007	2008	2009	CAGR
Jerónimo Martins	**1.636**	**2.295**	**3.398**	**3.596**	**30%**
Metro	2.065	2.531	2.851	2.381	5%
Tesco	1.454	1.963	2.187	1.936	10%
Schwarz G.	1.184	1.556	2.069	1.924	18%
Carrefour	1.039	1.516	1.887	1.579	15%
Others	37.589	41.329	47.446	42.425	4%
Total	**44.967**	**51.190**	**59.838**	**53.840**	**6%**

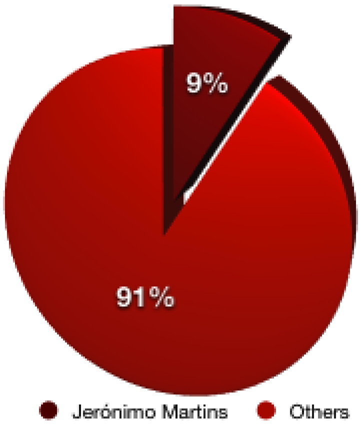
Source: Nova ER Team Estimates

As we can see in **Exhibit 11 A**, Jerónimo Martins (Biedronka) accounted for only 7% of the Polish MGD market in 2009, albeit the fact that it dominated 70% of its segment (Hard-discount). Biedronka was also able to expand its sales at a CAGR of 30%, an impressive performance that was well above the second largest retailer (Metro Group) and the overall market.

Despite the fact that the Polish market was fiercely hit in 2009, with overall sales decreasing by approximately 10%, we highlight the fact that Biedronka was able to grow its sales by 6% YoY[8].

[8] Sales already converted to the Euros. In local currency (Zloty) the sales have grown 29.8% YoY and 8.3% LFL.

Exhibit 11 B – Market Share (2015)



Source: Nova ER Team Estimates

Growth prospects

The Polish market was showing a solid growth till 2009, with sales growing at CAGR of 15% in the previous 3-year period. Despite the 10% decline in sales last year, we believe the market will return to its previous growth rates as Poland recovers from the recent crisis.

Our optimism lies on three factors: i) excluding last year, the Polish grocery market was growing at double digits, ii) decrease in the "wealth gap" between the country and its European peers due to the fact that the Polish economy is expected to outperform the Euro-zone in the following years and, iii) convergence of the Polish retail market to the Western European standards.

We summarize our forecasts for the Polish Modern Grocery Market in the following table:

Exhibit 13 – Polish MGD market forecasts

	2010E	2011E	2012E	2013E	2014E	2015E	CAGR
Biedronka	**4.267**	**5.012**	**5.798**	**6.497**	**7.220**	**7.969**	**13.3%**
Others	58.922	63.665	69.198	73.950	78.728	81.868	6.8%
Total	63.189	68.677	74.996	80.447	85.948	89.837	**7.3%**
Market Share	**6.8%**	**7.3%**	**7.7%**	**8.1%**	**8.4%**	**8.9%**	

Source: Nova ER Team Estimates

Conclusion: we expect the Polish grocery market to expand its sales at a CAGR of 7.3% in the following five years, with Biedronka growing at an impresive CAGR of 13.3% according to our sales model.

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Operational Forecasts

A. PORTUGAL

Retail Mainland

In the last five years the Retail Mainland operations have been able to expand its sales area from 279.842m² (2004) to 434.744m² last year, representing a CAGR of 11.6%. Additionally, its sales grew at a CAGR of 12.8% in the same period.

According to our forecasts, the Retail Mainland unit will slowdown its expansion pace through a reduction in *Pingo Doce* new openings. The sales area will expand at a modest CAGR of only 0.2%, while the *Adjusted Sales per Square Meter*[9] should grow at a CAGR of 3.9% until 2020, well below the unit's previous performance.

Exhibit 14 – Sales Model (Retail Mainland)

	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Store Openings	10	7	6	7	3	2	
Closures	10	0	0	0	0	0	
Number of Stores	**343**	**350**	**356**	**363**	**366**	**383**	
Sales Area ('000sqm)	434,7	435,1	418,6	425,3	428,1	444,276	**0.2%**
Growth (%)	0.4%	0,1%	-3,8%	1,6%	0,7%	0,4%	
Adj. Sales per SQM[10] (€ k)	**6.06**	**6.59**	**7.01**	**7.43**	**7.85**	**9.32**	**4.0%**
Growth (%)	(5.7%)	8,8%	6,4%	6,0%	5,7%	1.9%	
Sales (€ mn)	**2.615**	**2.746**	**2.810**	**3.040**	**3.233**	**3.983**	**3.9%**
Growth (%)	8.2%	5,5%	2,4%	7,7%	6,4%	2.3%	

Source: Company Data and Nova ER Team Estimates

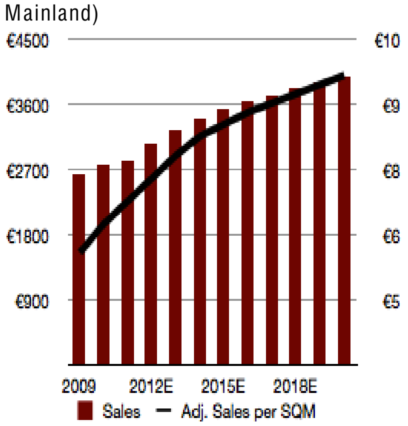
We are particularly optimistic with the Feira Nova's restructuring process...

We are particularly optimistic with the company's intentions to restructure its *Feira Nova* operations, a process that involves a gradual decrease in the non-food range and further integration under the *Pingo Doce* banner. The first conversion happened in Braga, while the second one is scheduled to open in Mem Mertins (Sintra) in the ending of this year, with the remaining seven hypermarkets being all converted in 2011.

We believe this restructuring process will bring strong benefits for the Retail Mainland operations due to: (i) decrease in the company's dependence on macroeconomic cycles, (ii) lower operating costs caused by a decrease in the sales area and, (iii) conversion into a much stronger and successful brand (Pingo Doce).

Recall that the hypermarket operations were deeply affected by the competition coming from Sonae MC (LFL +0.8% YoY), with Feira Nova's *like-for-like* sales dropping 16% last year. Nevertheless, the hypermarkets' larger focus in non-food goods also make it more susceptible to macroeconomic cycles, which also explains, though not completely, the negative performance during the recent crisis.

Exhibit 15 – Sales forecasts (Retail Mainland)



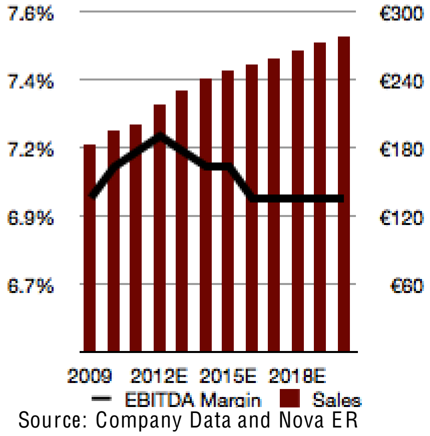
Source: Company Data and Nova ER Team Estimates

[9] Our model takes into account the fact that the opening of a new store does not have an immediate impact in the company's sales due to the time it takes to become fully operational
[10] Refer to previous footnote for methodology

Besides the increasing focus on food retail, the new stores will see its average area decrease from the initial 9.000 m² to 6.000 m², with the remaining area being converted in small shopping malls in order to enhance the potential number of clients visiting the stores.

Our model assumes slower growth rates for the *sales productivity* [11] due to two main factors: i) Feira Nova's restructuring effect should be partially offset by the decrease in the unit's aggressive expansion pace and, ii) the Portuguese retail market is already saturated, with M&A operations being highly unlikely to happen[12]. Additionally, we have assumed a higher growth rates in the next two years as the company fully integrates the former Plus stores, a process that we assumed to be completed in 2011.

Exhibit 16 – Sales vs. EBITDA margin forecasts (Retail Mainland)



Source: Company Data and Nova ER Team Estimates

In terms of **EBITDA margin** for the following years, we are once again particularly optimistic, especially considering that the company was able to increase that margin by 30bp in a deeply deflationary environment such as the one in 2009.

Even though we believe the worst of the deflationary environment have passed, analysts still expect low levels of inflation for the years to come. Together with the increasing competition coming from Sonae MC, we believe that Jerónimo Martins will have to fight hard to increase its EBITDA margin to the levels once achieved before the crisis.

However, we believe that the full integration of the Plus stores and the improvement in the Feira Nova's *sales productivity*[13] once restructuring is complete, will allow the Retail Mainland operations to gradually increase its EBITDA margin until it reaches 7.2% in 2012, then stabilizing around 7% in the long run.

Exhibit 17 – Retail Mainland Forecasts

(€ mn)	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Sales	**2.615**	**2.758**	**2.823**	**3.040**	**3.233**	**3.983**	**3.9%**
EBITDA	**183.1**	**195.8**	**201.8**	**218.9**	**231.2**	**278.8**	**3.9%**
EBITDA margin (%)	7.00%	7.10%	7.15%	7.20%	7.15%	7.0%	
Depreciation	**85.8**	**96.5**	**100.2**	**109.4**	**108.3**	**119.5**	**3.1%**
EBIT	**97.2**	**99.3**	**101.6**	**109.4**	**122.9**	**159.3**	**4.6%**
EBIT margin (%)	3,7%	3,6%	3,6%	3,6%	3,8%	4.0%	

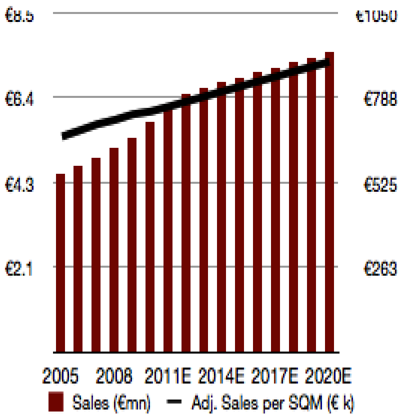
Source: Company Data and Nova ER Team Estimates

Recheio

We highlight the fact that the Cash & Carry chain of Jerónimo Martins was able to survive the recent crisis without posting negative sales growth in any of the past

[11] According to company data, Pingo Doce achieved €6.3k sales per SQM in 2009, while Feira Nova's average sales per SQM were only €3.7k in the same period. Refer to footnote 7 for methodology
[12] See **"Does Minipreço really make sense…"** in this report for further details
[13] Refer to footnote 7 for methodology

Exhibit 18 – Sales vs. Sales productivity forecasts (Recheio)



Source: Company Data and Nova ER Team Estimates

3-years. Since 2006 the wholesaler managed to grow its sales at a CAGR of 5.0%, while its *sales productivity* grew at a CAGR of 2.4%. **In anticipation of the difficulties in both the segments it operates (Traditional Retail and HoReCa) and the recent deflationary environment, the unit focused on the reinforcement of its customers' competitiveness and the launching of a private brand for the Traditional Retail**. Additionally, we expect Recheio to increase the number of stores to 40 in the next three years and then remain stable until 2020. Recall that even considering that Recheio emerged stronger from the recent crisis, the market is still a highly mature one, with no room left for significant growth. Therefore, we expect Recheio to increase its sales area at a CAGR of only 1.4% in the next ten years. In terms of sales productivity, we forecasted a moderate CAGR of only 1.8%, reflecting both a saturated market and a weaker demand**.**

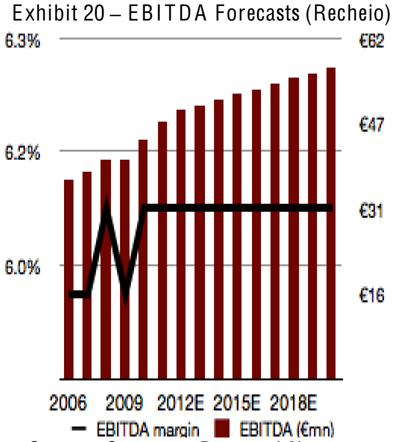
Concluding, we expect sales to grow at a CAGR of 3.1%, below its recent performance and only slightly above the long-term inflation rate of 2% in Portugal[14].

Exhibit 19 – Sales Model (Recheio)

	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Store Openings	0	2	2	1	0	0	
Closures	0	0	0	0	0	0	
Number of Stores	**35**	**37**	**39**	**40**	**40**	**40**	
Sales Area ('000sqm)	114,410	122,766	129,402	132,720	132,720	132,720	**1.4%**
Growth (%)	(1.1%)	7.3%	5.4%	2.6%	0.0%	0.0%	
Adj. Sales per SQM[15] (€ k)	**5.95**	**6.02**	**6.14**	**6.27**	**6.39**	**7.26**	**1.8%**
Growth (%)	2.4%	1.2%	2.1%	2.0%	2.0%	1.9%	
Sales (€ mn)	**664.8**	**710.8**	**764.8**	**800.3**	**816.2**	**927.5**	**3.1%**
Growth (%)	5.3%	6.9%	7.6%	4.6%	2.0%	1.7%	

Source: Company Data and Nova ER Team Estimates

Exhibit 20 – EBITDA Forecasts (Recheio)



Source: Company Data and Nova ER Team Estimates

Regarding EBITDA margin, we expect it to increase by 10 bps this year and then remain stable over the following years. Overall, EBITDA is expected to grow at a CAGR of 2.7% in our 10-year forecast period.

Exhibit 21 – Recheio Forecasts

(€ mn)	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Sales	**664.8**	**710.8**	**764.8**	**800.3**	**816.2**	**927.5**	**3.1%**
EBITDA	**39.9**	**43.4**	**46.7**	**48.8**	**49.8**	**56.6**	**3.2%**
EBITDA margin (%)	6.0%	6.1%	6.1%	6.1%	6.1%	6.1%	
Depreciation	**8.0**	**9.9**	**10.7**	**11.2**	**12.2**	**13.9**	**5.2%**
EBIT	**31.9**	**34.1**	**35.9**	**37.6**	**37.5**	**42.7**	**2.7%**
EBIT margin (%)	4.8%	4.8%	4.7%	4.7%	4,6%	4,6%	

Source: Company Data and Nova ER Team Estimates

[14] Recall that all CAGR are Nominal growth rates, which means they already include the expected inflation rate
[15] Refer to footnote 7 for methodology

Madeira

According to our forecasts, the business will suffer a slowdown due to the floods that recently hit the island, which led to the temporary closure of two supermarkets.

We expect this impact to be only temporary, with the business unit back on track in the following years, in line with our previous forecasts.

Exhibit 22 – Sales Model (Madeira)

	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Store Openings	0	0	0	0	0	0	
Closures	0	0	0	0	0	0	
Number of Stores	**15**	**15**	**15**	**15**	**15**	**15**	
Sales Area ('000sqm)	14,626	14,300	14,300	14,300	14,300	14,300	**0.0%**
Growth (%)	(2.2%)	0.0%	0.0%	0.0%	0.0%	0.0%	
Adj. Sales per SQM[16] (€ k)	**9.15**	**8.95**	**9.17**	**9.35**	**9.55**	**10.95**	**1.6%**
Growth (%)	4.3%	(2.2%)	2.5%	2.0%	2.1%	1.9%	
Sales (€ mn)	**127.0**	**123.1**	**126.1**	**128.6**	**131.4**	**150.6**	**1.6%**
Growth (%)	5.25%	6.92%	7.59%	4.64%	2.0%	1.7%	

Source: Company Data and Nova ER Team Estimates

We expect a temporary decrease of 20 bps in the EBITDA margin this year...

We highlight the fact that this extraordinary event will certainly affect the current EBITDA margin, causing a decrease of 20 bps from 4.8% in the previous year to 4.6%. We then expect it to gradually increase until it remains stable around 5.0% in 2013.

Exhibit 23 – Madeira Forecasts

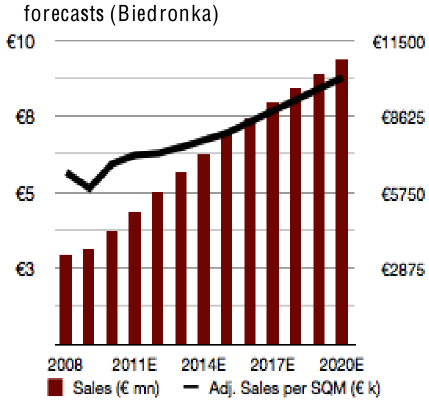
(€ mn)	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Sales	**127.0**	**123.1**	**126.1**	**128.6**	**131.4**	**150.6**	**1.6%**
EBITDA	**6.1**	**5.7**	**6.2**	**6.3**	**6.6**	**7.5**	**1.9%**
EBITDA margin (%)	4.80%	4.60%	4.90%	4.90%	5.00%	5.00%	
Depreciation	**0.5**	**1.0**	**1.4**	**1.5**	**1.7**	**2.1**	**13.4%**
EBIT	**5.6**	**4.7**	**4.8**	**4.8**	**4.9**	**5.4**	**(3.7%)**
EBIT margin (%)	4.3%	3.8%	3.8%	3.7%	3.7%	3.6%	

Source: Company Data and Nova ER Team Estimates

...and the business back on track in the following years...

Regarding sales, we expect the company to maintain the current sales area, with no store openings scheduled for the future in our sales model. The sales are expected to grow at a CAGR of 1.6% until 2020, below the 5.3% level exhibited between 2004 and the 2009.

Exhibit 24 – Sales vs. Sales productivity forecasts (Biedronka)



Source: Company Data and Nova ER Team Estimates

B. POLAND

Biedronka

Biedronka is currently the company's most valuable asset, accounting for 49% of its consolidated sales last year and approximately half of its reported EBITDA. **Management has recently unveiled its long-term prospects for Biedronka besides the 2.000 stores target for 2012, now setting the 3.000 stores as the new objective for 2020.** Given the company's past track record regarding its network expansion, we believe this is a perfectly reachable long-term objective.

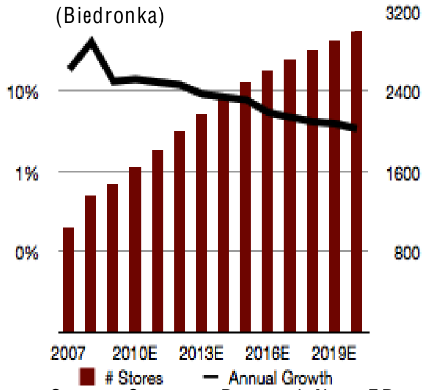
[16] Refer to footnote 7 for methodology

In Emergent Market, the percentage of stores in which the retailer actually own the space is particularly high, resulting in higher costs than if the company could simply rent the space. Poland is no exception and Biedronka currently owns 88% of its 1.466 stores. **Our model assumes a gradual improvement until the company is able to own only 50% of its stores in the long run, exactly the sort of weights between owned and leased stores we observe in more developed markets such as Portugal[17].** This had two consequences in our forecast model: i) reduction of Biedronka's operational costs and, ii) lower capital expenditures as the cost of a new store through leasing is 50% lower[18].

The weights between owned and leased stores equal 50% in mature markets...

We highlight the fact that the partnership Biedronka has celebrated with its suppliers implies that they have constant knowledge of the company's expansion plans, so that they can be ready and participate in such decisions. Consequently, we believe Biedronka's aggressive expansion plans were already discussed and "approved" by its suppliers.

Exhibit 25 – # Stores Evolution (Biedronka)



Source: Company Data and Nova ER Team Estimates

Concluding, we expect the company to fulfil its business plan concerning the network expansion, increasing the number of stores by 697 until 2012 and boosting its sales area at a CAGR of 12.4%. We then forecast a significant slowdown in the company's expansion pace until it reaches 3.000 stores in 2020, which will decrease the sales area's CAGR to 5.8% in that 8-year period.

Exhibit 26 – Sales Model (Biedronka)

	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Store Openings	163	170	178	186	160	90	
Closures	(53)	0	0	0	0	0	
Number of Stores	**1.466**	**1.636**	**1.814**	**2.000**	**2.160**	**3.000**	
Sales Area ('000sqm)	852,6	971,6	1096,2	1226,4	1338,4	1926,4	**7.7%**
Growth (%)	13.1%	14.0%	12.8%	11.9%	9.1%	3.4%	
Adj. Sales per SQM[19] (Pln k)	**22.3**	**23.8**	**25.4**	**27.1**	**28.8**	**40.6**	**5.6%**
Growth (%)	7.0%	6.7%	7.1%	6.6%	6.2%	4.3%	
EUR/PLN	**4.16**	**3.98**	**4.09**	**4.32**	**4.44**	**4.85**	**1.4%**
Adj. Sales per SQM[20] (€ k)	**5.13**	**5.97**	**6.22**	**6.28**	**6.48**	**8.38**	**4.6%**
Growth (%)	(9.1%)	16.3%	4.2%	0.9%	3.3%	4.9%	
Sales (€ mn)	**3596.5**	**4266.6**	**5012.3**	**5798.3**	**6496.8**	**10671.5**	**10.4%**
Growth (%)	5.8%	18.6%	17.5%	15.7%	12.0%	5.0%	

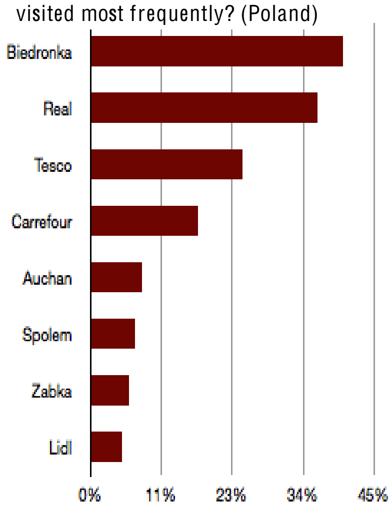
Source: Company Data and Nova ER Team Estimates

In terms of EBITDA margin, we expect an increase until it reaches 7.5% in 2012, then our model assumes it will gradually decrease to 7.1%, a long-term range slightly higher than the one provided by the company.

Our optimism lies on three factors: (i) an increase in the Biedronka's scale, (ii) lack of strong competition and (iii), expansion in Private Label products.

[17] According to company data the weights are precisely 50% in the Portuguese market
[18] The average cost of a new Biedronka store is €1.6mn if the company owns the space and only €0.8mn otherwise
[19] Refer to footnote 7 for methodology
[20] Refer to footnote 7 for methodology

Exhibit 27 – What is the shop you visited most frequently? (Poland)



Source: PMR Research

We recall here that Biedronka already has 60% of its offer as Private Label products, which we assumed to increase its growth potential both in sales and EBITDA margins.

The Private Label products are gradually increasing their market share in Poland due to three main factors: i) toughening economic conditions, ii) the rising availability of such products and, iii) increasing confidence regarding their quality. Additionally, the economic downturn has also pushed many Polish consumers towards limiting expenditure even on basic and non-essential goods, making private label products an increasingly popular option. According to a recent study issued by Planet Retail, the Polish Private Label market accounted for 11% of the Modern Grocery Distribution sales in 2009, well below the 34% market share we observe in Portugal and the 40% in Germany.

Therefore, **we expect the Private Label retail market to remain growing at double digits in the following years as the market converges to the Western European standards.**

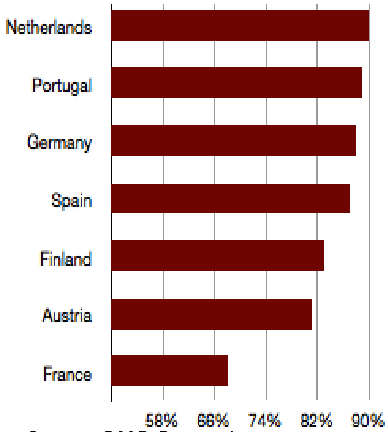
Exhibit 28 – Biedronka Forecasts

(€ mn)	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Sales	**3.596**	**4.267**	**5.012**	**5798**	**6.497**	**10.671**	**10.4%**
EBITDA	**262.5**	**315.7**	**370.9**	**434.9**	**487.3**	**779**	**10.4%**
EBITDA margin (%)	7.3%	7.4%	7.4%	7.5%	7.5%	7.1%	
Depreciation	**68.4**	**81.1**	**95.2**	**116.0**	**130.0**	**149.4**	**9.8%**
EBIT	**194.1**	**234.7**	**275.7**	**318.9**	**357.3**	**586.9**	**10.6%**
EBIT margin (%)	5.4%	5.5%	5.5%	5.5%	5.5%	5.5%	

Source: Company Data and Nova ER Team Estimates

Conclusion: hard-discount operations account for 8% of the overall retail market, with Biedronka currently dominating 70% of that segment. Given the fact that it has already achieved the larger scale by far within its segment, we believe that Biedronka will keep outperforming the market and competitors in the following years.

Exhibit 29 – Private Label Acceptance rate by country



Source: PMR Research

Industry

We recall that in difficult economic environments such as Portugal's one, in which costumers experience a significant erosion of their purchasing power and become extremely price sensitive, private label assumes an essential role through their low cost profile. Due to the expected decreasing disposable incomes, we expect the Portuguese customers to reduce their expenditure in *premium* products, therefore increasing the competition faced by the Industry business.

Therefore, we have assumed cautious forecasts, with sales growing at a CAGR of only 2.3% until 2020, slightly above the expected long term GDP growth.

Exhibit 30 – Industry Forecasts

(€ mn)	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Sales	**229.6**	**231.0**	**235.5**	**240.3**	**246.4**	**293.9**	**2.3%**
EBITDA	**35.1**	**35.1**	**35.8**	**36.3**	**36.7**	**42.9**	**1.8%**
EBITDA margin (%)	15.3%	15.2%	15.2%	15.1%	14.9%	14.6%	
Depreciation	**3.4**	**3.0**	**3.3**	**3.1**	**2.7**	**4.7**	**3.0%**
EBIT	**31.7**	**32.1**	**32.5**	**33.2**	**34.0**	**38.2**	**1.7%**
EBIT margin (%)	13.8%	13.9%	13.8%	13.8%	13.8%	13.0%	

Source: Company Data and Nova ER Team Estimates

Industry should be affected by Private Label's competition....

In terms of EBITDA margins we expect the unit to remain the most profitable one since costumers are always willing to pay a higher price for a premium brand they are familiar with. We also expect the EBITDA margin to gradually decrease due to the fierce competition from Private Label, until it remains stable around 14.6%.

Services

We expect Services to grow its sales at a CAGR of 4.3%, mostly due to the expansion to new formats.

Exhibit 31 – Services Forecasts

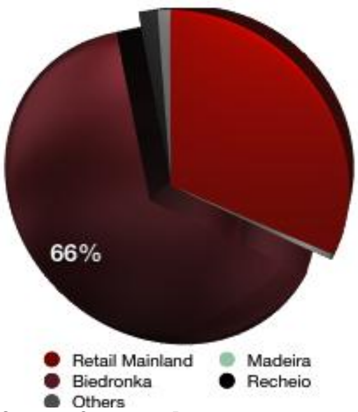
(€ mn)	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Sales	**84.2**	**87.2**	**89.3**	**94.8**	**100.2**	**138.1**	**4.6%**
EBITDA	**1.3**	**1.9**	**2.0**	**2.1**	**2.2**	**3.0**	**7.7%**
EBITDA margin (%)	15.3%	15.2%	15.2%	15.1%	14.9%	14.6%	
Depreciation	**1.7**	**1.8**	**1.9**	**2.0**	**2.1**	**2.9**	**4.6%**
EBIT	**(0.4)**	**0.1**	**0.1**	**0.1**	**0.1**	**0.1**	**n.a.**
EBIT margin (%)	(29.4%)	0.1%	0.1%	0.1%	0.1%	0.1%	

Source: Company Data and Nova ER Team Estimates

In terms of EBITDA margins we expect them to remain perfectly stable around the 2.2% in the medium and long term.

Addressing the cost of growth

Exhibit 32 – Capex Breakdown (2009)



Source: Company Data

The company recently unveiled its capex plans for the next three years, with an investment around €1.3Bn. We believe this investment plan is slightly optimistic and, according to our own forecasts, Jerónimo Martins will spend approximately €1.4Bn assuming the 2.000 stores target for Biedronka in 2012.

Our model have assumed three sorts of Capital Expenditures for Jerónimo Martins: (i) Expansion, (ii) Revamping, (iii) Conversion and, (iv) Distribution Centers. **Recall that the Conversion capex is merely temporary as the company still focuses on the former Plus stores conversion, a process we assumed to be completed by 2011**. Regarding Industry & Services we assumed a capex in order with company's own estimates.

Exhibit 33 – Capital Expenditures Forecasts

(€ mn)	2010E	2011E	2012E	2013E	2014E	2020E	CAGR
Distribution Centers	40.0	40.1	40.2	29.2	30.1	24.7	(4.7%)
Expansion	232.0	246.5	268.6	224.8	232.5	152.2	(4.1%)
Revamping	111.9	122.7	134.7	159.0	170.4	245.6	8.2%
Conversion	47.9	97.2	0	0	0	0	
Industry & Services	5.0	5.1	5.2	5.3	5.4	6.1	2.0%
Total Capex	436.7	511.7	448.7	418.3	438.4	428.6	(0.2%)
Capex/Sales	5.3%	5.7%	4.4%	3.8%	3.7%	2.7%	

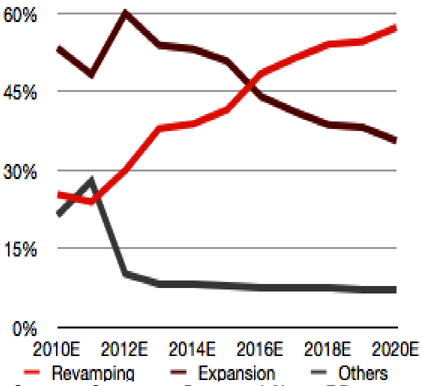
Source: Company Data and Nova ER Team Estimates

Biedronka should account for the majority of the Capex in the following years....

Last year the company reported that Biedronka accounted for 58.4% of the overall investment of €312.0 mn. We expect that share to suffer a significant increase as Jerónimo Martins focuses its attention in the Polish market, with **Biedronka expected to account for 66% of the overall investment in 2010.** Recall that our model assumes Biedronka will grow its sales area at a CAGR of 12% in the following three-year period, which will increase the capital expenditures until it reaches 5.7% of sales in 2011. Since we have assumed a significant deceleration of Biedronka's network expansion from 2013 onwards, the *Capex to Sales* ratio is expected to gradually decrease until it reaches 2.7% in the end of our forecast period.

Additionally, we expect the *Revamping Capex* to increase at a CAGR of 8.2% as the company increases the number of stores it operates and, consequently, has to increase its refurbishments. According to our model the *Revamping Capex* will finally overcome the Expansion one in 2016 (see **Exhibit 34**).

Exhibit 34 – Revamping vs Expansion Capex



Source: Company Data and Nova ER Team Estimates

We summarize our conclusions in **Exhibit 35**:

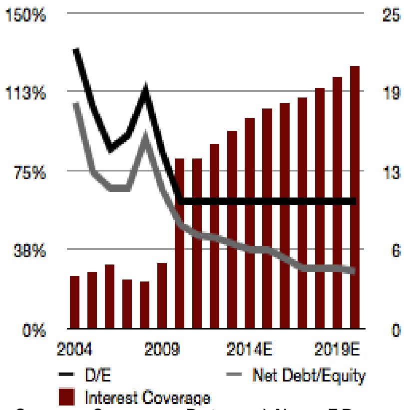
Exhibit 35 – Capital Expenditures Breakdown - Forecasts

	2010E	2011E	2012E	2013E	2014E	2020E	CAGR
Retail Mainland	131.4	179.2	88.6	85.3	87.6	113.4	(1.5%)
Biedronka	289.9	316.6	345.4	320.1	337.7	300.3	0.4%
Recheio	7.8	8.2	6.9	5.1	5.2	5.8	(1.5%)
Madeira	2.6	2.6	2.6	2.5	2.6	2.9	1.1%
Industry & Services	5.0	5.1	5.2	5.3	5.4	6.1	2.0%
Total Capex	436.7	511.7	448.7	418.3	438.4	428.6	(0.2%)

Source: Company Data and Nova ER Team Estimates

De-levering process...

Exhibit 36 – Leverage Position



Source: Company Data and Nova ER Team Estimates

As Jerónimo Martins' scale continues to be build, especially in its Polish operations, the company will be able to dilute the large investments made in store openings and distribution centers.

The reduction in capital expenditures related to expansion, together with continued working capital improvements, should allow Jerónimo Martins to proceed with an aggressive delivering process.

In terms of Working Capital we assumed the company will receive from customers in 9 days, whereas paying its suppliers in 102 days in 2010. In the long term we expect the company to achieve a *receivables turnover* of 8 days and a *payables turnover* of 104. We were also optimistic regarding *Inventory Turnover*, assuming the company will achieve a 20 days inventory period, which will then gradually decrease until it stabilizes around 18 days.

We expect further improvements in NWC...

The reason behind our optimism lies in two main factors: (i) the company's past performance, improving 8 working capital days since 2004 and, (ii) the increase in the company's scale, leading to higher bargaining power over its suppliers and customers.

Exhibit 37 – Net Working Capital Breakdown

	2004	2005	2006	2007	2008	2009	Long Term
Inventory Period	27.7	28.9	26.4	26.0	25.2	20.6	18
Receivables Turnover	11.8	12.6	11.5	10.5	9.2	9.5	8
Payables Turnover	103.9	105.4	107.6	108.7	101.8	101.5	104
NWC in Days	(50)	(49)	(53)	(57)	(54)	(58)	(62)

Source: Company Data and Nova ER Team Estimates

The company should achieve better creditor terms in the future...

Recall that we have assumed Jerónimo Martins to improve its creditor terms in our ten-year forecast period**. As mentioned, the continued improvement in the company's financial and liquidity position should allow it to achieve a significant reduction in its Cost of Debt**.

Exhibit 38 – Leverage Position Breakdown

	2009	2010E	2011E	2012E	2013E	2020E	CAGR
Net Debt	689.3	676.2	700.4	652.0	601.0	562.4	(1.8%)
Net Working Capital	(1.161)	(1.296)	(1.435)	(1.602)	(1.776)	(2.750)	7.8%
NWC in days	(58)	(58)	(58)	(58)	(59)	(62)	
Gearing (%)	65%	57%	52%	45%	40%	33%	
Interest Coverage	5.1	13.3	13.2	13.7	14.4	19.3	13.5%

Source: Company Data and Nova ER Team Estimates

Even though the macroeconomic picture in Portugal is getting darker over the past few months, we believe that this **de-levering process** is not directly related with such economic deterioration.

Biedronka generates most of the company's Free Cash Flow...

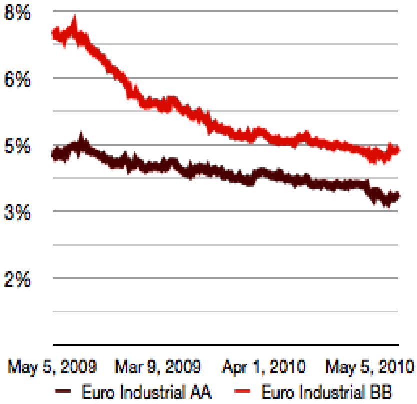
We highlight the fact that, despite the aggressive expansion in Poland, Biedronka has already achieved a great deal of consolidation, leading to strong generation of Cash-Flows that allow it to finance its own expansion without the need of support from the Head Office.

...and reduction in the Cost of Debt

We used Moody's methodology for Retail companies...

According to our initial analysis the company had a pre-tax Cost of Debt of 5.85% for its Portuguese operations and 6.96% for Biedronka[21]. However, these estimates were too conservative as we expect the company to improve its financial and liquidity position in the following years, leading to an expected lower cost of debt.

Exhibit 39 – BFV EUR Industrial rates



Source: Bloomberg

Due to the expected improvement in the company's financial health, we decided to compute a *synthetic rating* for Jerónimo Martins based on the methodology used by Moody's[22]. We conducted a quick and straightforward analysis of commonalities and differences in the credit ratings assigned to comparable companies in order to find the appropriate pre-tax Cost of Debt for Jerónimo Martins.

In order to attribute such rating we took into account *six key rating factors*, which were then divided into different sub-factors, each one with different weights. After computing a rating for each of the sub-factors (see **Appendix- Rating Methodology** for further details) we achieved the following results:

Exhibit 40 – Moody's Rating Methodology

Rating Factors	Sub-Factors	Weights	Ratings
Business & CF Volatility	Product Volatility	6.0%	**Aa**
	Geographic Diversification	4.0%	**A**
	Seasonality of CFOs	3.0%	**A**
Market Positioning	Scale	10.0%	**Baa**
	Market Share & Comp. Position	10.0%	**A**
	Cost Efficiency and Profitability	6.5%	**A**
Execution Ability	Quality of Merchandising	5.0%	**Aaa**
	Supply Chain	7.0%	**Aa**
Real Estate Assets Positioning	Investments in Store Quality	2.5%	**B**
	Barriers to Entry	5.0%	**B**
Financial Policy / Liquidity		8.0%	**Aa**
Key Indicator Ratios	Debt/EBITDA	8.0%	**Aa**
	RCF/Net Debt	8.0%	**Aa**
	EBITDA/Interest	7.0%	**Aaa**
	FCF/Net Debt	3.0%	**Aaa**
	CFO/Debt	7.0%	**Aaa**

Source: Moody's "Global Retail Industry"

Our analysis led to a Synthetic Rating of A...

Conclusion: Jerónimo Martins has an overall implicit rating of *A*, which allows us to compute the correspondent Cost of Debt using the BFV Euro Industrial rates for such rating taking into account the 10 year forecast period of our analysis (see **Exhibit 39**).

Exhibit 41 – Moody's Rating Methodology

Ratings	Weights	Dist. of Scores	Weighted Score	Indicated Rating	Overall Score
Aaa	22.0%	1	0.22	Aaa	1.49 or lower
Aa	37.0%	3	1.11	Aa	1.5 to 4.49
A	23.5%	6	1.41	**A**	**4.5 to 7.49**
Baa	10.0%	9	0.90	Baa	7.50 to 10.49
Pre-Tax Cost of Debt	**4.12%**[23]			***Overall Score***	**4.77**

Source: Moody's "Global Retail Industry"

[21] Source: Company Data and Analyst Estimates
[22] Moody's *Rating Methodology –" Global Retail Industry", 2006*
[23] Arithmetic Average of the last one year period using daily data

Valuation Summary

We analyzed each of our DCF assumptions with a significant impact in our Price Target of €8.12/sh...

In terms of **Betas**[24], we divided the companies further analyzed at **Comparables** into two different sub-groups: (i) European retailers with exposure to Emergent Markets and, (ii) European retailers with low or even no exposure at all to Emergent Markets. Biedronka was valued using the first group, while the Portuguese operations remained with the second one.

We updated our Market Premium assumptions for both Portugal and Poland....

Even though we believe the market is currently overreacting regarding the probability of default for Portugal, we believe that the **Market Premium** assumed in the previous analysis is now a too conservative one given the darker macroeconomic picture. We recall that the Market Premium reflects fundamental judgments we make about how much risk we observe in the Economy and what is the price that comes attached to such observed risk. If the Market Premium rises, then investors will immediately charge a higher price for that risk and demand to pay lower prices for the same set of risky expected cash flows. Therefore, we calculated the **Country Risk Premium** using the 10 year Credit Default Spreads adjusted for the Volatilities of both the Equity Index and the country's 10 year bonds[25]. Finally, as a proxy for **Risk-free,** we used the 10-year German Sovereign Bond for Portuguese operations and the 10-year Polish Sovereign Bond when valuing Biedronka's operations[26].

We summarize our Discounted Cash-Flow (DCF) assumptions in **Exhibit 42**:

We expect the domestic operations to grow in line with long term inflation...

Exhibit 42 – DCF Assumptions

	Portugal	Madeira	Poland	Terminal Growth Rates	
Risk-Free	**3.2%**	**3.2%**	**5.8%**	**Retail Mainland**	**2.0%**
Mature Market Premium [27]	4.0%	4.0%	4.0%	Real Growth Rate	0.0%
Country Premium	2.3%	2.3%	3.2%	Long Term Inflation	2.0%
Market Premium [28]	**6.3%**	**6.3%**	**7.2%**	**Recheio**	**2.0%**
Beta Unlevered [29]	0.53	0.53	0.50	Real Growth Rate	0.0%
Beta levered [30]	0.77	0.77	0.75	Long Term Inflation	2.0%
Cost of Equity [31]	**7.8%**	**7.8%**	**9.6%**	**Madeira**	**2.0%**
Pre-tax Cost of Debt	4.2%	4.2%	4.7%[32]	Real Growth Rate	0.0%
Tax Rate	26.5%	25%	19%	Long Term Inflation	2.0%
After-tax Cost of Debt	**3.1%**	**3.1%**	**3.8%**	**Biedronka**	**2.5%**
Target D/E	**60%**	**60%**	**60%**	Real Growth Rate	0.0%
D/(D+E)	**38%**	**38%**	**38%**	Long Term Inflation	2.5%
WACC [33]	**6.2%**	**6.2%**	**8.4%**	**Ind. & Services**	**2.0%**

Source: Nova ER Team Analysis

[24] The beta of each company in the industry was calculated as $\boldsymbol{Beta_i = Cov(R_i; R_{Market)}/Var(\sigma_{Market})}$, using 4 years of weekly data

[25] We expect the Country Risk Premium to be higher than the country default risk spread, so: $\boldsymbol{Market\ Premium = CDS\ spread * \text{Equity Index Volatility} / \text{Bond HoldingReturns Volatility}}$

[26] Since its cash flows are in the local currency (Zloty)

[27] We assumed to be 4%, which is in line with current financial theory

[28] Basically, we assume that $\boldsymbol{Equity\ risk\ premium = Mature\ market\ premium + Country\ risk\ premium}$

[29] $\boldsymbol{\beta_{unlevered} = \beta_{levered} /(1 + \frac{D}{E} * (1 - T_c))}$, assuming the Beta of debt as zero

[30] Using the same formula mentioned in the previous footnote

[31] $\boldsymbol{R_{levered\ equity} = Risk - free + \beta_{levered} * (Market\ Premium)}$

[32] Part of Biedronka's debt is in Zlotys, which is not linked to the *Euribor* rate. After discussion with the company's Investor Relations Office, we have assumed the unit pays 50 bps higher for its Debt

[33] $\boldsymbol{WACC = (\frac{E}{D+E} * R_{levered\ equity} + \frac{D}{D+E} * Cost\ of\ Debt * (1 - T_c))}$

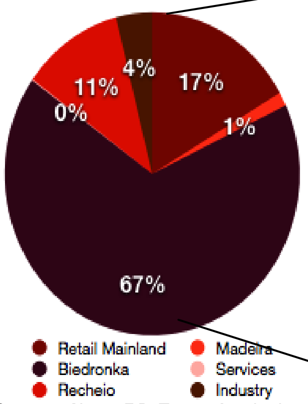
Sum-of-the-Parts

Finally, we are now able to value Jerónimo Martins using the *sum-of-the-parts* valuation method in order to consolidate all the six units we have analyzed so far. As shown in **Exhibit 42**, we assumed all the Portuguese operations to have a terminal growth rate in line with the expected long-term inflation rate of 2% per annum.

Our base scenario does not include the Polish Euro adoption....

In Poland we decided to proceed cautiously, with the terminal growth rate being set in line with our inflation forecast of 2.5%. **We recall that our base scenario does not incorporate a possible adoption of the Euro in Poland, which would decrease the expected inflation rate to the one set by the European Central Bank, among several other impacts**. This means we are not incorporating any possible expansion benefits in our valuation of Biedronka, therefore assuming there will be no store openings from 2020 onwards.

Exhibit 43 – S-o-P Breakdown



Source: Nova ER Team Analysis

Exhibit 44 – Sum-of-the-parts Valuation Breakdown

	EV	Stake	Attrib. To JM	%
Retail Mainland	1.778	**51%**	907	17%
Recheio	605	**100%**	605	11%
Madeira	100.1		76	1%
Retail Portugal	**2.484**	**75,5%**	**1.588**	**29%**
Industry	477	**45%**	215	4%
Services	14		7	0%
Industry & Services	**491**	**51%**	**222**	**4%**
Retail Poland	**3.664**	**100%**	**3.664**	**67%**
Enterprise Value			**5.454**	**100%**
Consolidated Net Debt			(676)	
Debt Attributable to Minorities			251	
Financial Investments			72	
Equity Value			**5.101**	
Shares (mn)			**628**	
Price Target			**€8.12**	

Source: Nova ER Team Analysis

We also highlight the fact that Biedronka accounts for 67% of our S-o-P valuation, which means Jerónimo Martins is now much more levered to the dynamics of the Polish market than to its highly mature domestic market.

Peer group comparison

We have also cross checked our *sum-of-the-parts* valuation with market multiples associated with comparable companies. The idea behind such rationale is to compare JMT with its peers taking into account two sorts of peer groups: (i) **Eastern and Central European** food retailers that exhibit significant growth prospects due to their exposure to emergent markets similar to Poland and, (ii) **Western European** food retailers, whose growth prospects are at least limited since they are mostly exposed to mature markets with high penetration rates such as the Portuguese one.

We compared Jerónimo Martins with other retail companies...

In order to compute the *implicit price* through *Multiple Comparison* we have attributed to the Emergent retailers the same weight we applied to Biedronka in our *sum-of-the-parts* valuation (see **Exhibit 43**).

By applying the 67% weight to the Emergent Retailers we have achieved the following conclusions:

Exhibit 45 – Relative Valuation

	EPS					P/E				EV/EBITDA			
	10E	11E	12E	13E	CAGR	10E	11E	12E	13E	10E	11E	12E	13E
Tesco	0.34	0.38	0.42	0.47	11%	14.7	13.3	11.9	10.6	9.6	8,7	8,1	7,2
Carrefour	2.33	2.78	3.19	3.64	16%	16.5	13.8	12.1	10.6	8.0	7,3	6,7	6,1
Metro	2.85	3.51	4.06	4.56	17%	15.8	12.8	11.1	9.9	5.4	4,9	4,4	4,2
Ahold	0.84	0.93	1.03	1.09	9%	12.0	10.8	9.8	9.2	6.0	5,7	5,4	5,2
Casino	5.09	5.72	6.25	6.73	10%	12.8	11.4	10.5	9.7	6.6	6,2	5,8	5,6
Sainsbury	0.26	0.28	0.31	0.35	10%	15.1	14.0	12.6	11.2	7.2	6,7	6,1	5,7
Delhaize	5.37	5.83	6.27	6.13	4.5%	11.5	10.6	9.9	10.1	5.6	5,3	5,0	5,0
Morrison	0.22	0.26	0.29	0.31	13%	14.7	12.8	11.6	10.7	7.9	7,1	6,5	6,1
Colruyt	10.30	11.24	12.07	13.14	8%	17.9	16.4	15.3	14.0	10.1	9,3	8,8	8,0
Mature					**11%**	**14.5**	**12.9**	**11.6**	**10.6**	**7.4**	**6.8**	**6.3**	**5.9**
X5 Group	1.02	1.45	2.00	2.43	34%	26.3	18.6	13.5	11.0	11.4	9.0	7.4	6.4
Magnit	3.26	4.25	5.31	6.63	27%	20.1	15.4	12.3	9.9	11.5	8.7	7.1	6.0
BIM	1.59	1.84	2.20	2.11	10%	26.1	22.3	18.1	18.9	17.2	14.3	12.4	11.5
Emergent					**23%**	**24.2**	**18.2**	**14.6**	**13.3**	**13.4**	**10.7**	**9.0**	**8.0**
Weighted Multiples					**19%**	**21**	**16.8**	**13.6**	**12.4**	**11.4**	**9.4**	**8.1**	**7.3**
Nova ER					**11%**	**20.0**	**17.7**	**15.7**	**14.3**	**9.1**	**8.2**	**7.3**	**6.7**

Source: Bloomberg Consensus

We highlight the fact that if we had used the *Bloomberg Consensus* EV/EBITDA from the Emergent category to value Biedronka we would get a new Price Target of €9.0/sh, which is 11% higher than ours.

JMT is trading at a premium with Western retailers...

Concluding, our *sum-of-the-parts* valuation seems to be in line with this relative valuation through Multiples. **According to our analysis Jerónimo Martins is trading at a premium compared to the Western retail sector, which we believe to be perfectly justifiable given its major exposure to Biedronka's impressive growth potential.**

...and at discount relative to retailers focused only on Emergent markets...

Regarding the Emergent category we observe precisely the opposite, which is also justifiable given their higher expected EPS growth for the next three-year period. Recall that we expect Jerónimo Martins to increase its EPS at a CAGR of 13% in the next four years, a number clearly above the Western retailers but still far away from Eastern and Central European retailers that are 100% focused on emergent markets.

Risks to our Analysis

We believe the main risk to our Valuation analysis would be the Euro adhesion of Poland, which would significantly change our Price Target in a way that we will further analyze in this report. Additionally, our valuation is also highly dependent on the evolution of the Zloty as it substantially impacts our DCF calculations for Biedronka.

In terms of Portugal the main risk would be a scenario in which the country would be forced to leave the European Union. Even though we are no experts in macro economy, we consider such scenario as highly unlikely to happen.

Does Minipreço really make sense...

According to information recently released by the Press, Carrefour is ready to sell its Minipreço stores and definitely exit Portugal after selling its hypermarkets to Sonae in 2007 for an Enterprise Value of €622mn.

Minipreço's underperformance would lead to a discount....

By analyzing the Western retailers, more specifically the ones with very low or no exposure at all to emergent markets, we get an average EV/Sales[34] Multiple of €0.46[35]. Since Minipreço had sales of €915mn, we would get an estimated Enterprise Value of €418mn for this deal. However, we highlight that Minipreço's underperformance (-6.9% LFL growth in 2009) should probably lead to a discount in order to attract potential buyers.

However, we believe Jerónimo Martins would not be interested in such deal for three main reasons: (i) the company is now focused in consolidating Poland and finding a new international market to expand to, (ii) regulators would certainly impose restrictions and, (iii) significant operational differences with Pingo Doce. Despite the fact that Jerónimo Martins could easily get the funds needed for such operation, we recall that the company recently unveiled its plans for an international expansion that will certainly be made through acquisitions, which could implicate a significant financial effort. Additionally, we also highlight that the 524 Minipreço stores have an average area of only 500m², which clearly contrasts with the average 950m² for the stores under the Pingo Doce banner. Finally, the regulator would certainly impose serious restrictions since Jerónimo Martins and Sonae MC already control 38% of the Portuguese Market.

The Minipreço stores have an average area of only 500m²...

...With 49% of JMR so close?

Exhibit 46 – EV Breakdown

Source: Nova ER Team Analysis

We are also sceptic regarding such deal since the company could get a higher return by simply acquiring the remaining 49% of JMR that belongs to the Ahold. According to our *sum-of-the-parts* valuation, the Retail Mainland Operations have an Enterprise Value of €1.778mn, which lead us to an EV/EBITDA of 9.1 considering its significant growth prospects. However, the EV/EBITDA Multiple we find in the market for retailers focused only on mature markets yields only 7.3, which means that Retail Mainland would then have an Enterprise Value of only €1.435, 19% lower than our own valuation.

Thus, we believe the company could buy the 49% stake for an EV significantly lower than its intrinsic value. Such deal would be made between the EV/EBITDA multiples we mentioned before, which lead us to an Enterprise Value between €703 and €871mn. Despite the fact that we observe a strong potential for value creation in this deal, we believe the company will not proceed with such operation as it implies a significant financial effort that could eventually compromise its international expansion through acquisitions.

[34] We used EV/Sales instead of EV/EBITDA since Carrefour does not disclose that such information
[35] Our analysis included the following companies: Ahold, Sainsbury, Delhaize and Morrison

Polish Euro Adhesion

As mentioned, we have not included such scenario in our analysis due to the impossibility of quantifying certain issues that would certainly cause a bias in our *sum-of-the-parts* valuation.

Poland's new possible target for Euro adoption is now 2015...

The **first issue** would be the year in which Poland would finally adopt the Euro currency. The previous Euro adoption target of 2012 was abandoned as the public deficit rose and the zloty tumbled with the financial crisis. **The Polish government recently mentioned 2015 as a possible new target date**. However, this data could be once again delayed as the European Union struggles to maintain stability and solving its own existent problems.

Recall that Poland's public deficit hit 7.2% of GDP in 2009 and is expected to be around 7% in 2010 as the government maintains high spending levels in order to keep the economy on track. According to the OECD, the macro-policy followed by the polish was largely appropriate as the sharp depreciation of the polish currency cushioned the impact of foreign shock, though it led to the consequent postponement of euro adoption.

It would be impossible for us to forecast the exact equilibrium exchange rate for the Euro Adhesion…

Secondly, it is impossible for us to accurately forecast the equilibrium exchange rate between the Zloty and the Euro in 2015. Even though we could assume the exchange rate observed in the market, we believe that would always be a noisy approximation. Recall that several economists have already criticised the exchange rate applied to Portugal, Spain, Ireland and Greece. Additionally, we believe the European Union will be particularly rigid in this issue so that it does not make the same mistakes that could eventually put the UE once again in danger of a possible breakdown.

Our Analysis

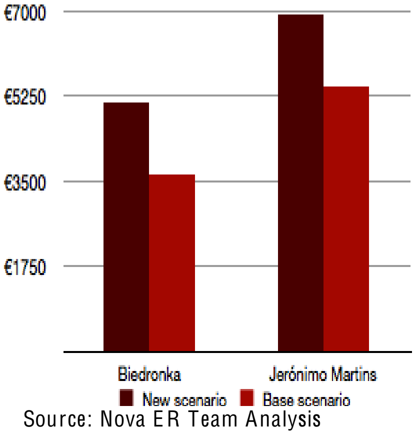
Even though we consider this scenario analysis as a simple approximation to reality, we decided to analyze the impact in our *sum-of-the-parts* valuation of a possible Euro adoption in 2015.

We divided Biedronka into two sorts of Cash Flows: before and after Euro adoption….

Besides assuming 2015 as the real target, we have also assumed the exchange rate of that year as the equilibrium one, which means it will remain the same from 2015 onwards. Recall that the EUR/PLN forward rates used to discount Biedronka's cash flows assumed a gradual depreciation of the Zloty against the Euro, meaning that a fixed exchange rate will always have a positive effect in our *sum-of-the-parts* valuation.

Then we divided Biedronka into two sorts of Free-Cash Flows: (i) until 2014 and, (ii) 2015 onwards, including the perpetuity. The second set of cash flows were discounted using a new WACC that reflected the necessary differences in both the Cost of Debt and the Risk-Free.

Exhibit 47 – Biedronka EV Scenario Analysis



Source: Nova ER Team Analysis

The Cost of Debt would be the same one applied in the Portuguese operations since Jerónimo Martins would no longer have part of its debt in Zlotys. Regarding Risk-free, we used the 10y German Government Bonds due to the fact that Biedronka's cash flows would then be in Euros instead of Zlotys.
Therefore, the first set of cash flows were discounted using our previous WACC of 8.4%, while in the second ones we have used a new WACC of only 6.6%[36]. **Additionally, the Terminal Value would then consider a Terminal Growth rate of 2%, 50 bps lower that our previous one, reflecting a long term inflation rate set accordingly to the European Central Bank's ambitions for the Euro countries[37].**

As we can see in **Exhibit 47**, Biedronka would increase its Enterprise Value by 40%, reflecting a stronger exchange rate and a lower WACC used to discount its Free Cash Flows.

Sensitivity Analysis

We also proceeded with a sensitivity analysis regarding the year in which Poland would finally adopt the Euro. As expected, a delay of the Polish Euro adhesion in our model decreases the Price Target from €10.45/sh (2015) to €10.11/sh if we assume Poland to adopt the Euro currency only in 2020. We summarize our findings in the following table:

Exhibit 48 – Sensitivity Analysis

	2015E	2016E	2017E	2018E	2019E	2020E
Biedronka EV	**5.108**	**5.058**	**5.022**	**4.967**	**4.928**	**4.899**
Total EV	6.918	6.868	6.833	6.777	6.738	6.709
Equity value	6.565	6.515	6.479	6.424	6.385	6.356
Implied Price Target (€/share)	**10.45**	**10.37**	**10.31**	**10.22**	**10.16**	**10.11**

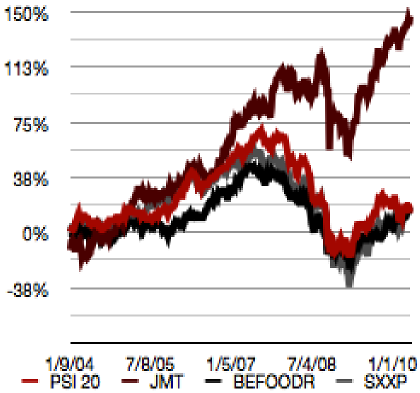
Source: Nova ER Team Analysis

Conclusion: Our Price Target would increase by 29% to €10.4 and the potential upside would then be 55% if Poland adheres to the Euro currency in 2015. As we delay such scenario in our model the impact on our *sum-of-the-parts* valuation is reduced until it represents an upside of 39% over the stock current price and 25% above our initial Price Target of €8.12/sh.

[36] Even though we have assumed the Market Premium to remain the same, this is not completely accurate since the adoption of the Euro would make Poland less risky, which would then lead to a lower market premium
[37] Recall that a lower inflation also decreases Jerónimo Martins' revenues due to its significant impact on the company's sales growth

Is Jerónimo Martins really creating value?

Exhibit 49 – Cumulative Returns



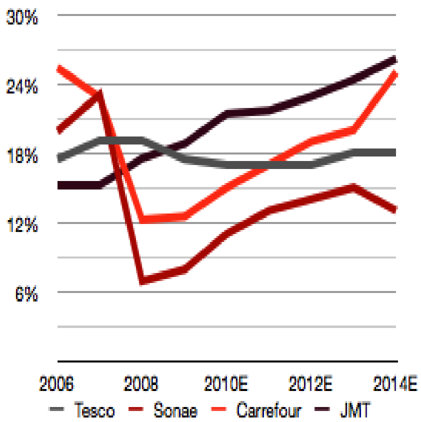
Source: Bloomberg

The purpose here is to infer if the company is really creating value when compared with the Market and Comparable companies.

We started by assuming that a firm whose stock has gone up is viewed as having created value, whereas one whose stock price has fallen has then destroyed value. As we can see in **Exhibit 49**, **the company clearly beat the Portuguese and European Indexes since 2004, achieving a cumulative return of 144%**[38]. Since the BEFOODR index already includes the main European retailers, we can also conclude that the company beat its competitors as well.

Even though the creation of value seems obvious, stock prices can fluctuate around the true value of a company for quite long time, which means that market returns can also be noisy.

Exhibit 50 – Return on Equity



Source: Company Data and Bloomberg Consensus

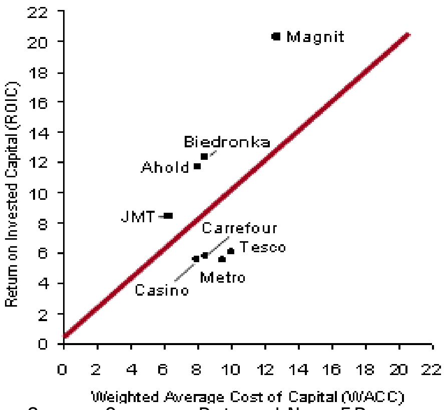
We have also analyzed the Return on Equity (RoE) ratios of both Jerónimo Martins and similar companies within the retail industry. **Though it seems obvious that Jerónimo Martins is creating value according to a RoE comparison (Exhibit 50), we highlight the fact that the differences may simply reflect different accounting standards between countries.**

Therefore, we have extended our analysis to the Return on Invested Capital (ROIC), which we believe to be critical when comparing the profitability of different companies across the same industry.

Since we valued Biedronka with a different cost of capital (WACC), we divided Jerónimo Martins into two different parts. Furthermore, we have considered Biedronka's invested capital in €500 mn last year, with the remaining amount (€1.255 mn) being related to Portugal[39].

Assuming that a company is creating value whenever its WACC is higher than the ROIC, we can observe in Exhibit 51 that Jerónimo Martins, both in Portugal and through Biedronka, is actually creating value. Magnit and BIM[40] had the higher creation of value among the industry due to their higher focus on Emergent market, where the growth prospects are far brighter than the ones faced by retailers struggling with their highly mature domestic markets.

Exhibit 51 – ROIC vs. WACC (%)



Source: Company Data and Nova ER Team Estimates

Conclusion: whatever criteria we had used in this analysis it seems obvious that Jerónimo Martins is in fact creating value, though it did not achieve the Value Creation exhibited by some of its Emergent peers.

[38] Price data adjusted for Dividends and stock splits;
[39] Using company data provided by the Investor Relations Office
[40] Despite the fact that it is not present in **Exhibit 51**, BIM had a ROIC of 45% against the 6% of its WACC

New Internationalization...

According to Jerónimo Martins' Chairman, Mr. Alexandre Soares dos Santos, the company is currently planning a new internationalization process after consolidating Poland and the failed attempt to enter the Brazilian retail market. The purpose here is to analyze the Brazilian retail market, the one management believed to have the best fit with the company's strategy and profile. Recall that Brazil was the market referred by Mr. Alexandre Soares dos Santos during a conference at *Universidade Nova de Lisboa* two months ago.

Market Size and Growth

Brazilian MGD market grew its sales at a CAGR of 11% in the last 5 years…

Retail sales in Brazil haven been expanding at robust growth rates until 2009, when the financial crisis led to a significant decrease in the growth pace achieved before. The resilient domestic consumption sustained the retail market last year, with consumers benefiting from improved income levels, leading to an increase in the Modern Grocery Distribution sales of 5% YoY.

Exhibit 52 – Brazilian MDG Market

	2006	2007	2008	2009	2010E	CAGR
Retail Sales (€ mn)	400.723	449.388	489.802	504.830	631.257	**12%**
Growth (%)	n.a.	12%	9%	3%	25%	
Retail Sales per capita(€)	2.159	2.395	2.583	2.636	3.266	**11%**
MGD sales (€ mn)	71.312	79.241	85.920	89.960	110.576	**12%**
Growth (%)	n.a.	11%	8%	5%	23%	
MGD Sales per capita (€)	384	422	453	470	500	**7%**

Source: TNS, Planet Retail and Nova ER Team Estimates

We expect the market to grow its sales at a CAGR of 16% in the next 5 years…

We expect the market to accelerate its growth from 2010 onwards, even achieving higher growth rates than the ones achieved before 2009. Our forecasts are based on: (i) the fact that food sales still account for 52% of the overall retail sales, well below the Western European standards we mentioned before, (ii) GDP Average Annual Growth rate of 4.4% until 2015, (iii) Population expected to increase from the 191 mn last year to approximately 200 mn in 2015, (iv) boom in credit availability and finally, (v) increasing consumer income levels. Based on our econometric model, the Brazilian Modern Grocery Distribution should yield a CAGR of 15% in the next five years.

We summarize our conclusions in the following table:

Exhibit 53 –Brazilian MGD market Forecasts

	2010E	2011E	2012E	2013E	2014E	2015E	CAGR
Retail Sales (€ mn)	631.257	757.684	874.111	993.538	1.112.965	1.243.392	**15%**
Growth (%)	25%	20%	15%	14%	12%	12%	
MGD sales (€ mn)	110.676	131.392	154.108	177.824	201.940	230.536	**16%**
Growth (%)	23%	19%	17%	15%	14%	14%	
GDP Growth	5.5%	4.1%	4.1%	4.1%	4.1%	4.1%	
Population (k)	193.253	194.933	196.525	198.043	199.492	192.492	**1%**
Inflation (%)	5.1%	4.6%	4.5%	4.5%	4.5%	4.5%	

Source: TNS, Planet Retail and Nova ER Team Estimates

We do not consider Brazil as an option for now…

Closed Market for now

Even though we recognize the Brazilian MGD market a high growth potential, we believe it would be practically impossible for Jerónimo Martins to replicate Biedronka's success. Despite the fact that the market remains quite fragmented, the market has three large players: Pão de Açucar, Carrefour and Wal-Mart[41].

We summarize the Market shares evolution of the first two retailers in the following table:

Exhibit 54 –Brazilian MGD market Breakdown

(€ mn)	2006	2007	2008	2009	CAGR
MGD sales	71.312	79.241	85.920	89.960	8%
Pão de Açúcar	5.085	5.600	6.781	8.432	18%
Market Share	7.1%	7.1%	7.9%	9.4%	
Carrefour	3.839	5.608	7.255	8.309	29%
Market Share	5.4%	7.1%	8.4%	9.2%	

Source: TNS, Planet Retail and Nova ER Team Estimates

Conclusion: Despite the fact the two market leaders control only 19% of the market, against the 38% we observe in Portugal, we recall that the Carrefour and Wal-Mart are international retailers with huge financial power when compared to Jerónimo Martins. Additionally, Pão de Açucar recently merged with another local retail giant, *Casas Bahia*, forming a retail group worth €19 Bn. Therefore, we believe the Brazilian Market is closed for now and the company should focus its attention on other markets.

[41] Unfortunately, Wal-Mart does not disclose its international sales, so we could not compute the Market Share

Possible IPO for Biedronka?

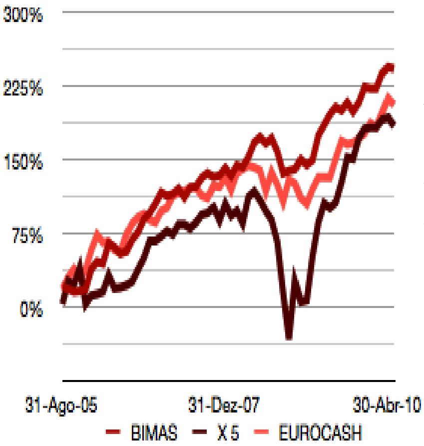
The company could use Biedronka's IPO as an option to raise cash…

Jerónimo Martins excellent fundaments and strong balance sheet should allow it to pursue an aggressive acquisition, if really necessary, in order to continue its internationalization process. Recall that we have assumed the company to reduce its Net Debt from €689 mn last year to only €159 mn in 2020, while the Debt to Equity ratio decreases from 112% in 2008 to a constant 60% in our valuation model. **Therefore, we believe the company could easily increase its leverage without risking its strong balance sheet and liquidity position.**

Biedronka might help

However, we highlight the fact the company could also proceed with an *Initial Public Offering* (IPO) of its Polish business unit, raising the cash needed to finance a significant acquisition without significantly increasing its leverage. Additionally, the company could also distribute the capital raised through an extraordinary dividend, though we consider such scenario as highly unlikely to happen.

Exhibit 55 – Cumulative Returns since IPOs (%)



Source: Bloomberg

As mentioned in the **Peer Group Comparison**, if we valued Biedronka through the Multiples we found for retailers focused on Emergent markets, our price target would be increased to €9.0/sh. This upside exists since Biedronka's Enterprise Value would climb from €3.6 Bn to €4.2 Bn, an increase of 16%.
Therefore, we believe Jerónimo Martins could raise the capital needed to pursue a growth strategy (through acquisitions) by simply using an IPO for its Polish business unit. Thus, if we assume the company could raise capital by the Multiples found in the market, then Jerónimo Martins could in fact create value through this operation, assuming here that the *true value* of Biedronka lies in the €3.6 Bn we applied in our *sum-of-the-parts* valuation.
Regarding the percentage of Biedronka the company would put in the market we have computed a simple sensitivity analysis[42]. We summarize our conclusions in the following table:

Exhibit 56 – **Sensitivity Analysis on Biedronka's IPO %**

	10%	20%	30%	40%	50%[43]
Implied Price Target (€/sh)	8.19	8.27	8.34	8.41	8.49
Implied Upside[44] (%)	12%	13%	14%	15%	16%

Source: Nova ER Team Estimates

Conclusion: we believe Jerónimo Martins would only use the IPO of Biedronka as a last resource option, in the case that a possible acquisition could endanger its Leverage and Liquidity position. We also highlight the fact that previous IPOs of retailers in the Eastern Europe have been a success, which strengthens our analysis (see Exhibit 55).

42 Assuming no transaction costs involved, which we considered to be only residual in this analysis
43 In fact we have assumed 49.99%, implying that the company would want to lose control
44 Assuming the price at 03/06/10 - €7.289/sh

Appendix

Rating Methodology

Six key rating factors:

- ***Business and CF volatility***
- ***Market positioning of the retailer***
- ***Execution ability***
- ***Real estate assets positioning***
- ***Financial Policies***
- ***Key indicator ratios***

Retailers exhibit different operational and financial dynamics due to the wide range of business models, segments and formats that exist in the global retail industry. The JMT's peers we have considered are the same ones we have analyzed in **Comparables**, with the slightly difference that only part of them actually have an available public rating.

1. Business and Cash Flow volatility

1.1 Product Volatility

Exhibit 57

sub-ratings	Description
Aaa	Food retailer selling staple products only
Aa	Food retailer with limited non-food offer
A	Food retailer with large non-food offer
Baa	DIY / Home appliances/Auto parts
Ba	Music and books/Consumer electronics
B	Specialty apparel/Toys
Caa	Specialty luxury items with low brand recognition

Source: Moody's

The rationale behind this sub-factor is to analyze the fashion/product renewal risk, which is critical for retailers focused on non-food goods. Taking this into account we have attributed an ***Aa*** rating on this sub-factor since a large share of its revenues come from food related goods.

1.2 Geographic Diversification

Despite the success of Biedronka the international expansion of JMT is still limited...

Here, we focused our attention on the differences between countries since companies such as JMT can offset the impact of macroeconomics' cyclicality by being present both in mature markets (low growth prospects) and certain emergent markets (high growth prospects). This sub-factor implies considerable geographic diversification for the higher sub-ratings and, in order to maintain some conservationism in our analysis, we have decided to attribute JMT a rating of **A** instead of ***Aa*** since its international exposure is currently limited to its Polish operations.

Exhibit 58

Sub-ratings	Seasonality of CFOs
Aaa	At least 50% of sales generated from at least 10 international countries
Aa	At least 30% of sales generated from at least 5 international countries
A	**Mostly a national retailer, highly diversified within domestic market**
Baa	Operates in one country with significant national coverage
Ba	Local operator with > 100 stores
B	Local operator with > 50 stores
Caa	Local operator with < 50 stores

Source: Moody's

1.3 Seasonality of Cash Flow from Operations (CFO)

Using the CFO of Jerónimo Martins we are able to capture not only the impact of seasonality in the company's revenues but also in its working capital. The rationale behind this sub-factor is to measure the company's risk of ending up with too much stock or, on the other hand, with a stock crisis that inhibits it to satisfy customers' demand.

Exhibit 59

Sub-ratings	Seasonality of CFOs
Aaa	No seasonality
Aa	26-30% CFOs in a single quarter
A	30-40% CFOs in a single quarter
Baa	40-50% CFOs in a single quarter
Ba	50-60% CFOs in a single quarter
B	60-80% CFOs in a single quarter
Caa	Single quarter >80% of CFOs

Source: Moody's

In order to satisfy this requirement we have computed the Cash Flow from Operations of the last two years regarding each single quarter, in order to measure the seasonality inherent to those cash flows. According to the following table, assuming once again a conservative analysis, JMT has an ***A*** rating in this sub-factor.

The company exhibits a low level of seasonality regarding its Cash Flows from Operations...

Exhibit 60

	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09
EBIT	56.0	69.6	91.7	85.6	60.9	72.5	115.7	106.9
D&A	35.9	38.0	40.8	40.5	41.0	40.9	42.7	40.4
Interest Expenses	24.8	19.3	17.6	23.5	17.5	17.6	18.1	17.2
∆ NWC	33.4	38.4	65.5	49.9	26.0	32.1	36.2	41.6
Income Taxes	8.2	10.4	19.3	8.2	7.3	12.4	18.7	17.3
CFO	**92.2**	**116.3**	**178.5**	**107.8**	**103.1**	**97.9**	**157.7**	**154.4**
% of Total	**19%**	**24%**	**36%**	**22%**	**20%**	**19%**	**31%**	**30%**

Source: Company Data and Nova ER Team Estimates

2. Market Positioning of the Retailer

This rating factor considers the existing market position of a retailer as an accurate indicator of the company's ability to face future credit shocks such as the recent banking crisis.

Exhibit 61

Sub-ratings	Revenues
Aaa	> USD 200 billion
Aa	USD 75 to 200 Billion
A	USD 25 to 75 billion
Baa	**USD 7.5 to 25 billion**
Ba	USD 1 to 7.5 billion
B	USD 375 million to 1 billion
Caa	<USD 375 million

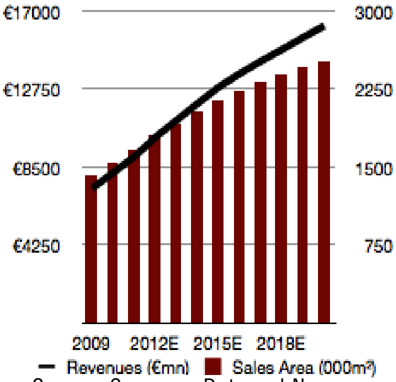
Source: Moody's

2.1 Scale (Revenues)

This sub-factor is quite straightforward since the company had revenues of €7.3 billion in the last year. Additionally, we expect the company to grow its sales from €8.1 billion in 2010 to €16.2 billion in 2020, representing a CAGR of 7.5%, leading to a rating of ***Baa.***

2.2 Segmental Market Share and Competitive Position

Exhibit 62 – Revenues vs Sales Area



Source: Company Data and Nova ER Team Estimates

The objective here is to examine the market position of JMT within its segment (Food Retail) relatively to its main competitors, and also takes into account the competitiveness within the retail market. Furthermore, we have also examined here the concentration of players within their segment and the overall trend in market shares for the retailer, so that we can conclude if JMT's competitive position is sustainable in the long run.

According to our **Market Environment** analysis the company will remain the number one hard discounter in Poland, mostly due to its aggressive expansion plans and consequently scale, allowing it to maintain its unquestionable price leadership. We recall that we expect Biedronka's sales area to grow at a CAGR of 10.4% in the next ten years.

JMT is the #1 Polish retailer and the #2 in the Portuguese retail market....

Regarding Portugal, the company will continue to be the largest retail group in what market share is concerned. Recall that the Retail Mainland operation is expected to grow its sales at a CAGR of 3.9%, versus the 10.4% of Biedronka.

Concluding, and since the revenues are expected to growth above 10% only until 2012, then gradually decreasing its pace until stabilize around 5% (see **Financials – Revenues Growth**), we attributed a rating of ***A*** in this sub-factor.

Exhibit 63

Sub-ratings	Description
Aaa	Market Leader across multiple product lines and segments; static competitive environment; Concept is still growing and is demonstrably portable; Sales growth remains above 10% Unquestioned Price Leader
Aa	**Market leader in its segment; highly stable competitive environment; concept may be maturing, but growth potential still evident; Presence is acknowledged and factored heavily into competitors' strategy Exhibits strong price leadership**
A	Strong competitor, with market leader generally forced to react to and consider implications of strategy Stable competitive environment; still growing concept as it should have very limited geographic weakness Moderate price leadership
Baa	Solidly credible competitor that may need to rely on tactical promotions to maintain share in face of stronger players in core markets or segments; moderately changing competitive environment; concept generally mature and exhibit signs of competitive stagnation Little price leadership
Ba	Tactically competitive and generally price-promotional to maintain sales; moderately competitive in certain markets and product line niches; significantly changing competitive environment; concept mature and may be slightly eroding Price taking behavior evidenced
B	Minimal competitive presence; very significantly changing competitive environment; falling sales and no growth potential; long-term survival is questionable No pricing power except for very defensive promotions

Source: Moody's

2.3 Cost Efficiency and Profitability

In this sub-factor we have used once again a quite straightforward method by measuring it through *EBITDA Margins* in comparison to the relevant competitors. Unfortunately, most of the retail companies do not disclose their *EBITDA margins* for each country. Therefore, we compare the companies' consolidated *EBITDA margins* since these are the best proxy we can get.

Concluding, we decided to attribute a rating of ***A*** in this sub-factor.

3. Execution Ability

Even a retailer scoring the highest ratings in the previous sub-factors have to invest in developing and maintaining customer loyalty by ensuring that its logistics are efficient and correctly dimensioned in order to deliver the product to the consumer at the right place and time. The rationale behind such idea is that a retailer that is able to be both efficient and responsive to customer expectations will eventually benefit from higher revenue growth, allowing it to gain higher power over suppliers and then pass those benefits on to its customers, hence feeding a virtuous circle of growth and profitability

3.1 Quality of Merchandise

In this sub-factor we focused only in the company's retail operations....

In assessing this sub-factor we have used the ability of JMT to produce *like-for-like* (LFL) sales above relevant competitors[45] both in Portugal and Poland. In this analysis we ignore the Industry and Services' operations since Moody's focuses its attention only on the performance of the retailer's main operations in its Key Markets. Therefore, we have analyzed Jerónimo Martins' retail operations in Portugal and Poland separately.

[45] Regarding retailers present in more than one market, Moody's focuses on the performance of the company's main operations in its key markets

Portugal

Exhibit 64 – Portugal LFL sales

	2007	2008	2009
Pingo Doce	8.7%	11.2%	2.7%
Feira Nova	-2.0%	-3.7%	-10.7%
Recheio	3.6%	4.5%	1.7%
Madeira	9.1%	1.4%	1.1%
Sonae MC	**3.5%**	**0.9%**	**0.8%**
Minipreço	**n.a.**	**n.a.**	**-6.8%**

Source: Company Data

The company has been able to overcome its competitors in the last three years by sustainably achieving a higher *like-for-like* performance. Considering Feira Nova's hypermarkets performance, we recall that these operations are undergoing through a major restructuring process involving a transfer of focus from non-food goods to a food related products, therefore less dependent on macroeconomic cycles.

Poland

Regarding the company's polish operations, the main international competitors are Tesco, Carrefour[46], Metro and especially Lidl. Unfortunately, Lidl does not disclose any information regarding the like-for-like sales growth in its polish operations. However, recall that the German hard discounter is expanding at a much slower pace, accounting for only 365 stores in 2009 against the 1.466 of Biedronka. Due to this lack of similar scale we have to assume that the Lidl's like-for-like sales growth also remained well below the one showed by Jerónimo Martins' polish operations.

Exhibit 65- Poland LFL sales

	2007	2008	2009
Biedronka	21.1%	20.1%	8.3%
Tesco	**3.0%**	**3.0%**	**2.0%**
Carrefour	**n.a.**	**n.a.**	**2.0%**
Metro	**3.3%**	**7.0%**	**1.5%**

Source: Company Data

Concluding, since the company's LFL sales growth remained consistently 3% per annum above its main competitors, we have attributed the maximum rating in this sub-factor - ***Aaa***.

JMT had LFL sales growth consistently above its competitors both in Poland and Portugal....

Exhibit 66

Sub-rating	Description
Aaa	**LFL sales growth consistently >3% above peers**
Aa	LFL sales growth consistently 2 to 3% above peers
A	LFL sales growth consistently 1to 2% above peers
Baa	LFL in line with peers
Ba	LFL sales growth 1 to 15% below peers
B	LFL sales growth 15 to 2% below peers
Caa	LFL sales growth >2% below peers

Source: Moody's

3.2 Assessment of supply chain

Exhibit 67 – Inventory Turnovers

Company	2007	2008	2009
JMT	26.0	25.2	20.6
SONAE MC	**64.5**	**61.0**	**59.6**
Tesco	**15.7**	**18.2**	**18.9**
Carrefour	**36.5**	**36.7**	**33.2**
Metro	**50.2**	**48.9**	**49.9**
Casino	**34.1**	**47.0**	**48.4**

Source: Company Data

This sub-factor is a merely qualitative assessment of JMT's reliability and robustness in terms of supply chain, analyzing its ability to get the right stock at time to deliver it to its customers. Due to our inability to accurately quantify such analysis we relied on the company own analysis when compared with some its peers. Additionally, we proceeded with an analysis focused on the inventory turnover of JMT and its peers which, together with the company's analysis, allow us to attribute a rating for this qualitative sub-factor. Furthermore, we have only considered comparable companies with larger exposure to the emergent markets in order to provide a more accurate analysis.

JMT's inventory turnover is similar to Tesco and well below its other peers....

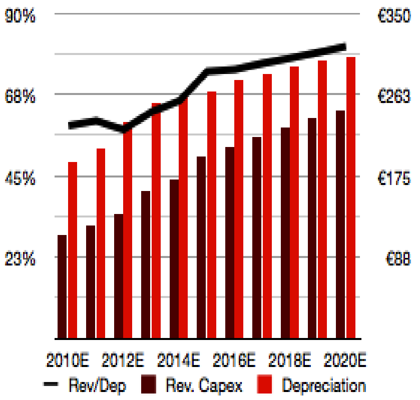
[46] Carrefour did not disclose its like-for-like sales growth for Portugal before 2009

According to our analysis JMT has an Inventory Turnover (in days) similar to Tesco, and well below the other peers. Considering this, we have decided to apply a rating of **Aa** to Jerónimo Martins in this sub-factor.

4. Real Estate Assets Positioning

A company's real estate portfolio is critical not only in operational terms, but also to the extent to which it can support or hinder future operational and financial performance, especially regarding the entry of new competitors.

Exhibit 68 – Revamping Capex and Depreciation



Source: Nova ER Team Estimates

4.1 Quality of store base

In this sub-factor we consider as a quantitative factor the Capital Expenditures budget tied to the relocation and refurbishment. The 3-year past average of Jerónimo Martins gross Capex (revamping) to Depreciation ratio yielded 92.7%, which would lead us to a rating of Ba.

However, we also took into account our forecasts concerning the Capital Expenditures tied to revamping for the 10-year period, which yields an average ratio of 69.5%. Based on these calculations we have decided to attribute instead a rating of **B** for this sub-factor.

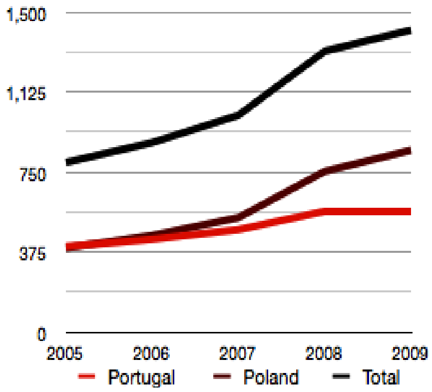
4.2 Barriers to Entry

This sub-factor is based merely on qualitative assessments...

In this sub-factor we took into account two different types if barriers to entry: Regulatory Barriers to Entry in Relevant Geographic Market and Cost of Real Estate Investments in the Relevant Geographic Market.

In Portugal, the retail market is already a saturated one, with the regulator increasing its pressure to limit new openings and further concentration among the major players. Recall that the regulator imposed serious restrictions when Sonae bought the Carrefour's hypermarkets in 2007, from limiting new stores openings in certain areas, to the sale of some previous existent stores.

Exhibit 69 – Capex by geography



Source: Company Data

In Poland the regulation is much more relaxed as regulatory requirements can be easily satisfied for most formats and operators. We recall that the company has increased its Polish sales area from 394.536m² in 2005 to 852.563m² in 2009, representing a CAGR of 21.2%.

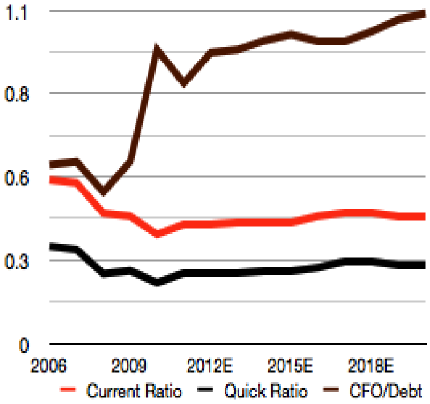
The Polish retail market has low barriers to entry when compared to Portugal...

According to Moody's own estimates, the Southern Europe usually ranks ***Baa*** in these sub-factors, while the emergent markets rank **Caa.** Since JMT is much more dependent on the Polish retail market we decided to attribute an overall rating of ***B*** in this sub-factor.

5. Financial Policies

This sub-factor focuses on the use of the company's cash flows, in particularly whether cash flows are returned to creditors or applied to enhance shareholder return.

Exhibit 70 - Liquidity Position



Source: Company Data and Nova ER Team Estimates

In terms of liquidity we have analyzed the company's liquidity position over the past 5 years and, despite the negative evolution of the *Current ratio*[47], it remains strong with the *Cash Flow from Operations* (CFO) being equivalent to 60% of the company's total debt in 2009.

Regarding shareholder returns we have used the most common ratio for such analysis, the Return on Equity, which climbed from 16.5% in 2005 to 18.8% in the last year. When compared with other retailers we expect JMT to outperform its peers in the following years (see **Exhibit 70**).

Concluding, we have attributed an overall rating of ***Aa*** in this sub-factor due to the expected improvement in the company's liquidity position and profitability.

Exhibit 71

Sub-rating	Description
Aaa	Very conservative; stable metrics, no "one-off" movements. Excellent Liquidity
Aa	**Stable and Predictable returns to shareholders; Creditors share equally in cash flow growth and proceeds from any asset sales. Liquidity is strong**
A	Predictable Share buybacks and acquisitions have minimal impact on metrics Possible event tied to acquisitions. Liquidity is strong
Baa	Financial Policies favor shareholder returns, possible track record of ratings migration following acquisitions. Liquidity is satisfactory
Ba	Clearly favorable to shareholders; Material debt-funded acquisitions and shareholders returns. Liquidity is satisfactory
B	Very focused on shareholders returns; Financial cushion may be paid out to shareholders ahead of business pressure. Liquidity is trained
Caa	Highly unfavorable to creditors: obligations close to default; Debt-restructuring likely .Liquidity virtually non-existent

Source: **Moody's**

6. Key Credit Metrics

This sub-factor is quite straightforward as it based on simple quantitative assessments. We summarize the *Key Credit Metrics* in the following table:

Exhibit 72

	Aaa	Aa	A	Baa	Ba	B	Caa
Debt/EBITDA	<1.25x	1.25-2.25x	2.25-3x	3-4x	4-5x	5-65x	>65x
RCF/Net Debt	>36%	30-36%	22-30%	14-22%	12-14%	8-12%	<8%
EBITDA/Interest	>10x	7-10x	5-7x	25-5x	15-25x	Jan 15, 2010	<1x per annum
FCF/Net Debt	>25%	18-25%	14-18%	12-14%	9-12%	0-9%	Negative
CFO/Debt	>35%	25-35%	20-25%	13-20%	9-13%	6-9%	<6%

Source: **Moody's**

The company exhibited a strong financial position in the previous year...

According to our forecasts, the company's financial position will improve as its *Capital Expenditures* budget tied to expansion gradually decreases in the following years, leading to a deleveraging process. Considering not only our forecasts but also the past performance of Jerónimo Martins, and once again

[47] $\mathit{Current\ Ratio} = \mathit{Current\ Assets}/\mathit{Current\ Liabilities}$

applying a very conservative analysis, we have achieved the following conclusions:

Exhibit 73

	2007	2008	2009	2010E	2011E	2012E	Sub-Rating
Debt/EBITDA	2.3	2.2	1.7	1.3	1.3	1.1	**Aa**
Retained CF/Net Debt	37%	31%	45%	61%	65%	57%	**Aa**
EBITDA/interest expenses	5.9	5.5	7.5	13.9	13.8	15.1	**Aa**
FCF/Net Debt	93%	58%	32%	52%	38%	65%	**Aaa**
CFO/Debt	56%	49%	58%	92%	81%	91%	**Aaa**

Source: Company Data and Nova ER Team Estimates

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Financial Ratios

	2009	2010E	2011E	2012E	2013E	2020E
Growth & Margins						
Revenues	6.1%	11.8%	10.7%	11.6%	9.1%	4.1%
EBITDA	11.6%	13.2%	11.0%	12.6%	8.9%	25.6%
EBITDA margin	7.2%	7.3%	7.3%	7.4%	7.4%	7.2%
EBIT margin	4.9%	5.0%	5.0%	5.0%	5.1%	5.2%
Net Profit	22.7%	27.7%	13.0%	12.3%	10.8%	4.2%
Profitability						
Gross Margin	19.0%	19.7%	19.7%	19.7%	19.7%	19.7%
Return on Capital Employed	18.1%	20.4%	20.4%	21.4%	22.1%	20.6%
Pre-tax RoIC	20.5%	21.7%	22.1%	24.1%	26.4%	37.1%
RoIC	16.4%	17.2%	17.6%	19.1%	20.9%	29.3%
RoE	18.8%	21.4%	21.6%	22.6%	23.3%	21.6%
Return on Sales	4.9%	5.0%	5.0%	5.0%	5.1%	5.2%
Liquidity						
Current Ratio	0.42	0.34	0.36	0.39	0.42	0.62
Quick Ratio	0.24	0.16	0.18	0.21	0.25	0.46
Working Capital	(1.161)	(1.297)	(1.435)	(1.602)	(1.776)	(2.750)
CFO/Debt	0.60	0.87	0.85	0.90	0.91	0.69
Leverage						
Debt/Assets	23.0%	18.0%	18.2%	17.9%	17.8%	18.9%
Debt Structure						
ST Debt/Debt	14.1%	12.0%	12.0%	12.0%	12.0%	12.0%
LT Debt/Debt	85.9%	88.0%	88.0%	88.0%	88.0%	88.0%
D/E	82.7%	60.0%	60.0%	60.0%	60.0%	60.0%
Net Debt/Equity	64.7%	56.7%	52.3%	45.4%	39.9%	33.4%
Debt/EBITDA (x)	1.67	1.20	1.21	1.15	1.14	1.31
Gearing (%)	64.7%	56.7%	52.8%	47.1%	39.6%	6.2%
Coverage Ratio (x)	5.11	13.26	13.16	13.72	14.10	12.79
Activity						
Fixed Assets Turnover	3.87	4.04	4.12	4.40	4.67	6.13
Inventory Turnover (days)	20.60	20.00	20.00	20.00	19.50	18.0
Receivables Turnover (days)	9.52	9.00	9.00	9.00	8.50	8.00
Payables Turnover (days)	101.5	102.0	102.0	102.0	102.0	104.0
NWC (days)	(58)	(58)	(58)	(58)	(59)	(62)
CFO/Capex	3.89	1.43	1.33	1.74	2.01	2.45
Capex/Depreciation	1.85	2.27	2.41	1.84	1.63	1.28
Capex/Sales (%)	4.3%	5.3%	5.7%	4.4%	3.8%	2.7%
Valuation						
P/E		19.95	17.65	15.71	14.18	9.29
EV/Revenues		0.67	0.60	0.54	0.49	0.34
EV/EBITDA		9.13	8.22	7.30	6.7	4.76
EV/EBIT		13.47	12.10	10.82	9.80	6.55
EV/Capital Employed		2.74	2.47	2.31	2.21	1.99
P/B		4.27	3.81	3.55	3.38	3.03
Dividend Yield (%)		50.0%	50.0%	70.0%	70.0%	70%
FCF Yield (%)		5.0%	4.6%	8.5%	10.7%	15.9%

Financial Statements (€ mn)

Consolidated Balance Sheet	2009	2010E	2011E	2012E	2013E	2020E
Tangible Assets	2.003	2.143	2.319	2.419	2.485	2.743
Intangible Assets	835	940	1.062	1.167	1.263	1.950
Other Non-Current Assets	214	220	235	263	318	895
Total Non-Current Assets	**3.052**	**3.303**	**3.616**	**3.849**	**4.066**	**5.588**
Inventories	334	360	398	444	473	640
Trade Debtors, Accrued Income an Deferred Costs	191	202	223	250	257	354
Other Current Assets	24	42	46	51	56	81
Cash & Cash Equivalents	223	72	128	217	347	1.400
Total Current Assets	**772**	**675**	**795**	**962**	**1.133**	**2.475**
Total Assets	**3.824**	**3.978**	**4.412**	**4.812**	**5.198**	**8.063**
Share Capital	629	629	629	629	629	629
Share Premium	22	22	22	22	22	22
Others	49	49	49	49	49	49
Retained Earnings	77	205	350	447	555	1.555
Minority Interests	288	288	288	288	288	288
Total Shareholders' Equity	**1.066**	**1.194**	**1.338**	**1.436**	**1.543**	**2.543**
Borrowings	756	630	707	758	815	1.343
Other Non-Current Liabilities	166	166	166	166	166	166
Total Non-Current Liabilities	**923**	**796**	**873**	**924**	**981**	**1.509**
Trade Creditors, Accrued Costs and Deferred income	1.647	1.835	2.031	2.267	2.474	3.698
Borrowings	124	86	96	103	111	183
Other Current Liabilities	64	67	74	82	89	129
Total Current Liabilities	**1.836**	**1.988**	**2.201**	**2.452**	**2.674**	**4.011**
Total Shareholders' Equity and Liabilities	**3.824**	**3.978**	**4.412**	**4.812**	**5.198**	**8.063**
Consolidated Income Statement	**2009**	**2010E**	**2011E**	**2012E**	**2013E**	**2020E**
Sales	**7.317**	**8.177**	**9.051**	**10.102**	**11.024**	**16.165**
EBITDA	**528**	**598**	**663**	**747**	**814**	**1.168**
Depreciation	(168)	(193)	(213)	(243)	(257)	(335)
EBIT	**360**	**405**	**451**	**504**	**557**	**833**
Net Financial Expenses	(70)	(31)	(34)	(37)	(39)	(65)
EBT	**279**	**374**	**416**	**467**	**517**	**768**
Income Taxes	(56)	(77)	(85)	(98)	(109)	(161)
Profit after Taxes	223	298	331	369	409	606
Minority Interests	(23)	(42)	(42)	(44)	(49)	(57)
Net profit	**200**	**256**	**289**	**325**	**360**	**549**
Consolidated Cash Flow Statement	**2009**	**2010E**	**2011E**	**2012E**	**2013E**	**2020E**
EBIT	360	405	451	504	557	833
Depreciation	(168)	(193)	(213)	(243)	(257)	(335)
Net Interest Expenses	(70)	(31)	(34)	(37)	(39)	(65)
Income Taxes	(56)	(77)	(85)	(98)	(109)	(164)
Δ NWC	136	136	139	167	173	107
Cash Flow from Operations	**527**	**626**	**682**	**779**	**840**	**1.049**
Net Capex	(304)	(437)	(518)	(466)	(440)	(532)
Net Financial Investments and Others	(16)	(7)	(8)	(10)	(33)	(12)
Minorities	(23)	(42)	(42)	(44)	(49)	(57)
Cash Flow from Investment	**(332)**	**(485)**	**(568)**	**(521)**	**(522)**	**(601)**
Dividends paid	(66)	(128)	(145)	(227)	(252)	(384)
Increase / (decrease) in Loans	(167)	(165)	87	58	65	99
Others	40	0	0	0	0	0
Cash Flow from Financing	**(193)**	**(293)**	**(58)**	**(169)**	**(187)**	**(285)**
Initial Net Debt	**821**	**689**	**676**	**707**	**676**	**222**
Δ in Net Debt	**(131)**	**(13)**	**31**	**(31)**	**(65)**	**(63)**
Net Debt	**689**	**676**	**707**	**676**	**611**	**159**

Disclosures and Disclaimer

Research Recommendations

Buy	Expected total return (including dividends) of more than 15% over a 12-month period.
Hold	Expected total return (including dividends) between 0% and 15% over a 12-month period.
Sell	Expected negative total return (including dividends) over a 12-month period.

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